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A SPECIAL REPORT

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Politics this week

Mar 15th 2007
From The Economist print edition

The Pentagon released an edited transcript of a closed-doors military hearing in which **Khalid Sheikh Mohammed** confirmed that he had masterminded the September 11th 2001 attacks. He also claimed involvement in a string of other terrorist acts and plots, such as the 1993 car bombing at New York's World Trade Centre, a failed plot to bomb Big Ben in London and attempts to kill Pope John Paul II and President Pervez Musharraf of Pakistan. The hearing took place at Guantánamo Bay to consider whether Mr Mohammed can be detained as an "enemy combatant". See article

The Democrats called for the resignation of America's attorney-general, Alberto Gonzales, when he admitted that mistakes had been made in last year's sacking of eight **United States attorneys**, who prosecute federal cases. White House officials were involved in the sackings, which the Democrats claim were politically motivated and not based on judicial performance. See article

George Bush asked for an additional 4,700 troops to join the "surge" in **Iraq**, on top of the 21,500 ordered to go in January. Meanwhile, agreement was finally reached in the Senate about the terms of the Democrats' resolution on Iraq, allowing debate to proceed.

Meeting and greeting

AP

George Bush completed his tour of five Latin American countries in which he talked of "social justice" and aid for health and education, as well as ethanol and immigration reform. He was greeted with small demonstrations by local left-wingers. **Hugo Chávez**, Venezuela's president, after a visit to Argentina where he called Mr Bush "a political corpse" at a rally, went on a seemingly improvised counter-tour of four countries. See article

Ecuador's conflict of powers continued. Police barred 57 opposition legislators from entering Congress after the electoral tribunal declared them expelled. At issue is a plan by Rafael Correa, the leftist president, to hold a referendum for a constituent assembly that would replace Congress. See article

In **Colombia**, a departmental governor from the opposition Liberal party surrendered to federal prosecutors investigating links between politicians and right-wing paramilitary groups. Eight other politicians, all supporters of President Álvaro Uribe, already face similar charges.

Whew!

Tony Blair faced the biggest Labour revolt in Parliament since the vote on the Iraq war in 2003. Some 95 backbenchers voted against renewing Britain's **Trident** nuclear-deterrent system. The prime minister, who is due to leave office this summer, won approval for his bill only with the support of the Conservative opposition. See article

Two **British soldiers** were acquitted of charges relating to the abuse of nine Iraqi detainees (one of whom died from his injuries) in Basra in 2003. Four other soldiers were acquitted last month. A seventh is due to be sentenced next month after pleading guilty.

Jacques Chirac announced that he would not stand again for the **French presidency**. The battle to succeed him is wide open, with the centrist François Bayrou now nipping at the heels of the two front-runners, Nicolas Sarkozy and Ségolène Royal. These three are some way ahead of the National Front's Jean-Marie Le Pen, who confirmed that he too is in the contest. See article

A huge demonstration against ETA, the Basque terrorist group, was staged in Madrid. The city also marked the third anniversary of the train bombings on March 11th 2004. Both events spelt trouble for **Spain's** prime minister, José Luis Rodríguez Zapatero, whose popularity has fallen sharply as voters see him as accommodating to terrorists. See article

United Russia, the main pro-Putin party, won 13 out of 14 regional elections in **Russia**. The 14th went to a new party, Just Russia, which is also loyal to President Vladimir Putin. See article

Mr Putin met **the pope** in Rome for the first time. Relations between the Roman Catholic and Russian Orthodox churches are strained. While he was in Italy, Mr Putin also finalised a bilateral gas deal with the Italian prime minister, Romano Prodi.

Security comfort blanket

Japan signed a security pact with **Australia** (its first such deal with a country other than the United States) to bolster co-operation on issues such as intelligence and border protection. The pact was interpreted by some as a response to China's growing power in the east Pacific. See article

Mohamed ElBaradei, who heads the IAEA, the UN's nuclear watchdog, described as “quite useful” talks held in **North Korea** on its recent promise to shut down its main nuclear reactor and close other facilities in return for fuel aid.

Nepal's prime minister, an erstwhile supporter of the country's monarchy, changed tack and suggested it would be better if the king were to abdicate. Last November's peace deal between the government and Maoist rebels agreed that the future of the monarchy should be decided after assembly elections this year.

In **India**, Naxalite rebels killed some 50 police officers when they stormed a security post in Chhattisgarh state, the most daring incident in a spate of recent attacks.

Muslim separatists were blamed for a gun attack on a minibus in southern **Thailand** that left nine people, all Buddhists, dead. The region has seen an increase in violence; some 2,000 people have been killed in the past two years.

Can't keep a good man down

AP

Riot police in **Zimbabwe** broke up an opposition rally, shooting dead one activist and arresting 50 others. One of those was Morgan Tsvangirai, the leader of the main opposition party, who was badly beaten in prison before being allowed to go to hospital. The episode was part of a pattern of increasing repression by President Robert Mugabe's embattled government in a week in which Zimbabwe's inflation rate reached 1,730%. See article

The first fully democratic presidential election since independence in 1960 took place in **Mauritania**. The run-off is due on March 25th.

The leaders of the **Palestinians'** rival Hamas and Fatah parties finalised the make-up of a new unity government. The key posts of finance, interior and foreign minister will go to men who are not members of either party.

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Business this week

Mar 15th 2007
From The Economist print edition

Viacom sued **Google** and its **YouTube** website, claiming they had a “brazen disregard” for the copyright of video and song clips that are uploaded by YouTube's users. The two sides failed to reach a distribution agreement earlier this year and Viacom is now claiming $1 billion in damages. It is the biggest challenge yet to the ability of “new” online media to use content produced by “traditional” media companies. See article

General Motors'restructuring plan seemed to bear fruit after it reported a net loss of $2 billion for 2006, improving on the $10.4 billion it lost in 2005. The carmaker even made a $950m profit in the fourth quarter as the performance of its North American operations picked up following cuts in production. Rick Wagoner, GM's boss, said that nobody was yet declaring victory.

The James Bond market

Ford found a buyer for **Aston Martin**, ending its 20-year control of the famous luxury-car brand. A consortium led by David Richards, an entrepreneur, and which includes two Kuwaiti investment firms, will pay £439m ($848m) for the British-based carmaker. With Ford trying to claw its way back from massive losses, analysts pondered whether it would need to sell other luxury brands, including Jaguar.

EADS, Airbus's parent company, confirmed that 2006 had been a dismal year when it reported net income had plunged by 94%, to *euro*99m ($124m). The turmoil in aircraft production at **Airbus** and a weak dollar were blamed for Airbus's first-ever operating loss. Louis Gallois, chief executive, gave warning of more poor results this year.

All charges were dropped against Patricia Dunn over the boardroom-spying scandal at **Hewlett-Packard**. Ms Dunn stepped down as the company's chairman last autumn after it was revealed that external investigators employed by HP had used false pretences to gain access to the private records of board members in order to flush out a leak.

A spanner was thrown in the works of the merger between the **Chicago Mercantile Exchange** and **Chicago Board of Trade** (CBOT) when the **Intercontinental Exchange**, an electronic futures and energy market, launched an unsolicited bid for CBOT.

Shopping spree

Kohlberg Kravis Roberts supported a £9.7 billion ($18.8 billion) buy-out bid for **Alliance Boots**, a British drugs retailer and distributor. Boots rejected the approach, led by its deputy executive chairman, but a higher offer is expected. KKR had more immediate success with **Dollar General**, a retailer that caters to low-income consumers. It agreed to be bought out by the private-equity firm for $7.3 billion. See article

Akzo Nobel, a Dutch conglomerate, surprised investors by agreeing to sell its pharmaceuticals business to **Schering-Plough** for $14.4 billion. Plans had been made for **Organon BioSciences** to float on the stockmarket.

Swisscom made a *euro*3.7 billion ($4.9 billion) offer for **Fastweb**, an Italian broadband provider. The Swiss telephone company's previous attempts at expansion have been frustrated by politicians at home. This time, it said, it has the backing of the state.

Cadbury Schweppes said it was separating its British-based confectionery and American-based beverages businesses and would provide more details in June. The announcement came after it was

revealed that Nelson Peltz, a shareholder activist, had taken a 3% stake in the company, which led to speculation about a buy-out.

Halliburton announced it was opening new corporate headquarters in Dubai. The move is meant to put the oil-services group closer to fast-growing oil-exploration and production areas, but some in Congress promised hearings.

Citigroup sweetened its bid for **Nikko Cordial**, a Japanese brokerage firm, increasing the value of its offer by a quarter, to $13.4 billion. Its decision came after the Tokyo Stock Exchange bucked expectations by deciding not to delist Nikko for inflating its earnings.

Feeling jittery

More bad news about America's **subprime-mortgage** market dented investor confidence again. The Mortgage Bankers Association reported a rise in mortgage defaults and activity in home foreclosures in the subprime market, which lends to borrowers with weak credit. Meanwhile, trading was suspended in **New Century Financial** after it indicated it faced bankruptcy; other subprime lenders showed increasing signs of being in financial trouble. See article

Anxiety about the banks' exposure to the subprime market and the knock-on effects on the economy fed volatility in **stockmarkets** around the world, which had only slightly recovered from a clobbering two weeks ago.

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KAL's cartoon

Mar 15th 2007
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Kevin Kallaugher

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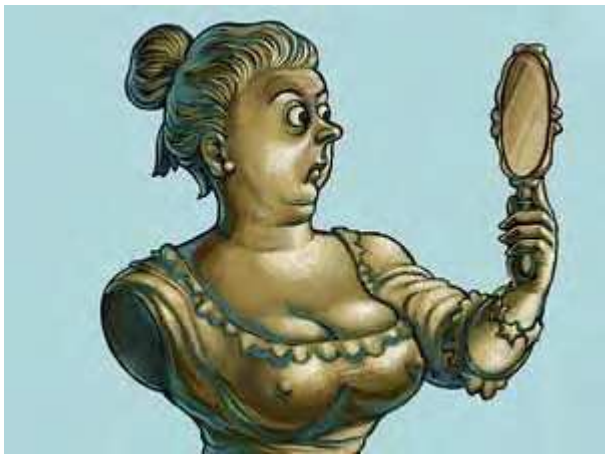
The European Union

Europe's mid-life crisis

Mar 15th 2007
From The Economist print edition

A successful club celebrates its 50th birthday in sombre mood

Jon Berkeley



ANYBODY reaching 50 naturally likes to reflect a bit on their achievements and failures. So it is with the European Union, which later this month marks the 50th anniversary of the signing in Rome of its founding treaty in 1957. Europe's leaders plan a jamboree in Berlin that will issue a portentous declaration. Their voters may not be impressed.

For the fact is that, even as it turns 50, the EU is mired in a mid-life crisis. The biggest problem is economic. European economies have perked up recently, but the record is still of lamentably slow growth and high unemployment. This is hardly the EU's fault—the blame lies more with national governments—but it makes it hard to drum up much popular affection for the union's institutions. Indeed, economic ills make voters suspicious not only of globalisation generally but also of such EU projects as enlargement and the single market. They also contributed heavily to the rejection of the EU's constitution by the French and the Dutch in 2005: France's voters might have said yes, had unemployment been 3%, not 10%.

In search of success

Does this sombre mood mean that the European project has failed? Not at all. As our special report this week notes, its early decades were spectacularly successful. The 50 years before the Treaty of Rome included two world wars and a great depression. The 50 years since have brought peace and prosperity on a scale unimaginable in Europe's history. This process culminated in 2004 in the reunification of a continent divided by the iron curtain of communism. Most European countries are now ensconced in the union.

But peace is now largely taken for granted. There is little enthusiasm for more enlargement, even though this has proved a brilliant way of entrenching liberal democracy in Europe's neighbourhood (more so than anything America has managed in its backyard). And, as for prosperity, young Europeans find it far less assured than it was for their parents.

The two big tasks for Europe's political leaders in Berlin ought thus to be clear. The first is to reinvigorate their economies. That requires painful changes to make labour markets more flexible, to trim overly generous welfare states and to inject new competition into product markets, especially for services,

which account for two-thirds of EU-wide GDP. To do all this means taking on trade unions and other vested interests. It also makes it vital for national governments to support, not undermine, Europe's single-market rules and competition policies. And it is thoroughly unhelpful if national politicians adopt the line that some candidates in France's presidential election have been taking by blaming the euro for their ills and bashing the European Central Bank.

The second job for the politicians is to make a lot more effort to persuade their voters that they have benefited from the enlargement of the club. All independent analyses of the expansion to take in central and eastern European countries in 2004 have found economic gains not just in the new countries but in the old ones as well—indeed, this is one reason why Europe's economies have recently picked up. Most pointedly, the gains were greatest in the three countries that fully opened up their labour markets to migrant workers from the new members: Britain, Ireland and Sweden. More such gains can be expected from any further enlargement.

Yet the Berlin meeting, under the chairmanship of Germany's chancellor, Angela Merkel, will be preoccupied by a different issue altogether: how to revive the draft EU constitution. Ms Merkel, whose country now occupies the union's six-monthly rotating presidency, has made this her overriding priority. Her reasoning is that the union cannot function properly without it, that due attention should be given to the 18 countries that have ratified the constitution and the four that are ready to do so, and that the EU can neither regain its zip nor expand any further unless the constitution is brought into effect in some form.

She is wrong. The EU's institutions were designed for six, not today's 27, and parts of the constitution would certainly improve them. But there is no agreement about what to do with the constitution. Some countries want a bigger treaty with social provisions; others a smaller one with no new powers for Brussels; others want to reopen all the institutional compromises. The French presidential election and the imminent arrival of a new British prime minister make agreement on a new text highly unlikely.

Anyway, the EU works without the constitution. It takes longer to make decisions with 27 than with six or 15, but that is not necessarily a bad thing. It is true that a new deal is needed by 2009 on the size of the European Commission and on votes and parliamentary seats for Croatia, but this can be done in Croatia's accession treaty. And the claim that no new members can sign up without the constitution is political, not legal. It is made by those who don't want Turkey to join and are using the constitution's absence as an excuse.

Enough bickering

Europe's disillusioned citizens are not interested in these institutional arguments in any case. In so far as they care about Brussels, they want not the constitution but simplification and more say in decision-making, which points to more radical answers. These might include scrapping such pointless bodies as the Economic and Social Committee and the Committee of Regions, replacing a European Parliament that cannot win legitimacy with a European Senate made up of national parliaments, and repatriating more powers back to nation-states. But what Europe's citizens want most of all from the EU is real benefits, especially economic ones.

An EU that helps to restore prosperity to its members may also be able to rekindle its citizens' enthusiasm for itself. Economic reform should thus make institutional reform easier to bring about. So can Europe resolve its mid-life crisis? Yes, if it concentrates on the things that matter most, instead of bickering over the constitution. The choice is between reform and revival or decline and decay.

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France's president

Jacques Chirac's poisoned legacy

Mar 15th 2007
From The Economist print edition

A long political career comes to a welcome end

AFP

Get article background

JACQUES CHIRAC, who has just announced his departure from politics, was first elected to parliament when Britain's Tony Blair was still at school; he first served as prime minister almost 33 years ago. As well as having plenty of political experience, he is an engaging man who likes nothing better than charming a roomful of voters. He has sometimes displayed great political courage: for instance, by speaking out against racism, acknowledging some of the darker episodes in France's history, such as its collaboration in the despatch of Jews to Nazi Germany, and supporting Turkey's bid for membership of the European Union.

Yet such points of light in Mr Chirac's presidency are notable mainly for their rarity. Many of the Western world's current and recently departed leaders are regarded as something of a disappointment; yet even in such company, Mr Chirac stands out as a failure.

Mr Chirac came to the presidency in 1995 vowing to heal France's “social fracture”, to cut youth unemployment and to improve the lot of ethnic minorities in the *banlieues*. He has fulfilled none of these promises. In his first term he half-heartedly backed the reforms of his prime minister, Alain Juppé, only to pull back at the first sign of street protests. This set a pattern for the next 12 years. Only last March, he disowned a labour-market reform proposed by the present prime minister, Dominique de Villepin. Today unemployment remains close to 9%, youth unemployment is over 20%—and the *banlieues* still simmer after the hot autumn of 2005.

Despite coming nominally from the right, Mr Chirac has acted as a president of the left (see article). Indeed, his 12-year tenure seems in many ways a continuation of the 14-year term of his Socialist predecessor, François Mitterrand. Neither had much time for America or the free market: Mr Chirac once denounced ultra-liberalism as the new communism. Both resorted to higher public spending and debt as an easy option to buy off bolshy voters. Neither cut the country's suffocating bureaucracy and tax burden. Both fought hard to keep European subsidies for France's cosseted farmers and to protect national champions.

Many French voters support Mr Chirac for his strong opposition to the Iraq war, which even made him briefly popular. Yet his aggressive tone strained relations not only with America and Britain, but also with eastern Europe. Even the boost for France's status in the Arab world proved fleeting. His indulgence of

Russia's Vladimir Putin was another black mark, and his loss of the May 2005 referendum on the EU constitution a personal failure. Elsewhere—in Africa, in Iran—Mr Chirac's freelance diplomacy and refusal to consult allies has been mostly just a nuisance.

But it is chiefly on his domestic policies that history will judge Mr Chirac; and that judgment is already being made. One sign of it is his low popularity rating, the worst of any president in the Fifth Republic. Another is the stink of corruption from his time as mayor of Paris, for which Mr Juppé was convicted in 2004. A third is his lack of an obvious successor, or even of much influence over the choice. He has ostentatiously failed to back his party's nominee, Nicolas Sarkozy, a man he heartily dislikes who is in effect running on an anti-Chirac ticket. The rise of the centrist François Bayrou has turned the presidential election into an open three-horse race. Whoever wins will inherit an unenviable legacy.

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Zimbabwe

Toppling a tyrant

Mar 15th 2007
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All Zimbabweans have reason to be rid of Robert Mugabe

AFP

JUST how much more misery and brutality can Zimbabweans take? Quite a lot, calculates Robert Mugabe, the country's thuggish 83-year-old president. He has just declared himself ready to stand in next year's election for another six-year term. The appalling beating inflicted this week on the main leader of the opposition, Morgan Tsvangirai, and other members of his Movement for Democratic Change (MDC) while they were in police custody shows how far Mr Mugabe and his henchmen will go to cling to power. Sadly, Zimbabwe's best hope is that the country's immiseration has gone so far that support for Mr Mugabe's misrule is now eroding even in his own ruling ZANU-PF party. Mr Mugabe has outfoxed opponents for 27 years, and may do so again (see article). But the outside world can help by making clear how a post-Mugabe government could end the country's isolation.

The latest violence came on March 11th when riot police prevented political, civic and church groups from holding a rally in support of political change. One activist was shot dead and Mr Tsvangirai and 50 others were arrested. Although divided, the opposition showed courage in bringing the resistance to Mr Mugabe's autocratic rule back onto the streets. But all Zimbabweans are now feeling the effects of the catastrophe that has overtaken the country.

Once the bread-basket of southern Africa and one of the continent's wealthiest countries, Zimbabwe is now a basket-case and suffers a severe shortage of food. It is also the world's fastest-shrinking peacetime economy, with unemployment now standing at 80%. Its inflation rate is the world's highest: currently 1,730%, although the IMF thinks that figure could rise to over 4,000% by year's end. From infant mortality to life below the poverty line, the country's unhappiest trendlines run remorselessly upwards. To stifle dissent and quash opposition, Zimbabwe has been turned into a police state where elections are routinely rigged.

The effect on ordinary Zimbabweans has been dreadful. Some 3m of them (out of a population of 13m) have fled the poverty and chaos of home, many to neighbouring South Africa. Despite all this, until now Mr Mugabe has been able to count on support from his rural heartlands. Yet even his backers there are being hurt by the scale of the economic collapse. And therein lies the hope.

There are reports of threatened rebellions in the army, the police and the civil service over derisory and irregular pay. Bigwigs in ZANU-PF with extensive business interests have seen their own fortunes hit by the rampant inflation. Economic embargoes imposed on Zimbabwe by America, Britain and others in response to Mr Mugabe's tyranny are taking their toll too. As a result, some factions within the ruling

party want Mr Mugabe to go in 2008, when his current presidential term ends. They then presumably hope to re-connect Zimbabwe with the foreign donors and financial institutions that could rescue it from decline.

The damage Mr Mugabe is doing to Zimbabwe is on such a scale that almost any opposition needs to be encouraged. But nudging him out will not be easy. He cares not a fig for what “neo-colonialists” in Britain and America might think of him, his methods or his ruinous economic policies. What his opponents need most of all, therefore, whether they are in the MDC or in ZANU-PF, is the backing and encouragement of their fellow Africans.

Devising the rescue

That has been conspicuously lacking. And it may be again. South Africa's response to the latest violence has been inaudible. The African Union, supposedly the continent's guardian of good governance, has likewise kept mum. Yet condemnation of what is happening in Zimbabwe by Mr Mugabe's peers would not only help loosen his grip on power, it would also set standards to which ordinary Zimbabweans could hope to hold a post-Mugabe government.

For there is a difficulty. Many erstwhile supporters who might see their own interests best served now by nudging the president aside have themselves done some of the plundering that has brought Zimbabwe to ruin. It is not enough therefore for outsiders simply to accept a “more moderate” successor from within the ruling party and let the regime return to tyranny as usual. Clear conditions need to be set for Mr Mugabe's successors to claim the aid and diplomatic support that could put Zimbabwe back on its feet. The first should be demonstrably free and fair elections as quickly as possible.

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Britain and the EU have learnt from some green-policy mistakes, but not from others

Satoshi Kambayashi

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ECONOMIC theory says that when an individual's choice damages others' interests, that damage should be reflected in the price he faces. The husky-hugging antics of David Cameron, the leader of the British opposition, who went off to the Arctic last year to watch it melting, may seem a long way from economic theory; but the greener-than-thou competition between Mr Cameron and Gordon Brown, who will probably become Britain's prime minister later this year (see article and article), along with the EU's environmental drum-banging at the European Council meeting last week (see article), are the political face of attempts to build that principle into economic policy. So far, those attempts to reduce the emissions that cause climate change have failed; but decisions by the European Union, announced on March 9th after last week's meeting, and by the British government, expressed in the climate change bill published on March 13th, suggest that both have learned from some mistakes, though not from others.

Governments can try to reduce emissions in three ways: subsidise alternatives, impose standards on products and processes and price the greenhouse gases that cause the damage. The first is almost always a bad idea; the second should generally be avoided; the third is the way to go. Europeans do all three. America does the first and the second at state and federal levels. California has decided to do the third, and it looks as though a federal system to price carbon will follow.

Green energy is fat with subsidies. America's ethanol subsidy, which has led to a huge rise in production, rocketing maize prices and consequent rioting in Mexico, is the sharpest example of why government should not pick winners: once the fertiliser and fuel used in corn production are taken into account, ethanol is probably not much greener than petrol. Europe has similarly daft subsidy regimes with equally perverse consequences—the German subsidy for solar energy, for instance, which has diverted the world's solar-cell production to sun-free Germany, thus raising the price in sunny countries where it might be usefully employed. Consumers pay for these indulgences through surcharges on electricity prices, but politicians like them, which is why the Europeans and the British both indicated there would be more of them.

There will also be more setting of standards. The EU plans to force companies to produce a certain proportion of the fuel they sell from renewable sources, and Britain proposes stricter standards for energy-efficiency in buildings. Sometimes market failure justifies setting such standards; but, like subsidies, they require governments to allocate resources, and markets are generally better at that than

are politicians or bureaucrats.

Neither subsidies nor standards should be needed if greenhouse gases are priced to reflect the damage they do. The EU's emissions-trading scheme (ETS), which caps the amount of greenhouse gases that factories may emit and gives them tradable allowances, is designed to do that. The principle is fine; but because governments handed out too many allowances, emissions have not fallen and the price of allowances has dropped from €34 ($42) per tonne of CO_2 at its peak a year ago to around €1.20 now—far too low to induce anybody to constrain their emissions. What's more, the scheme runs out with the Kyoto protocol, in 2012—too soon to affect industry's behaviour. If there's to be no carbon price after 2012, there's no reason for companies to invest in cleaner technology.

Green is groovy, but that may not last

The European Commission got tough last autumn, and slashed governments' allocation plans for the second phase of the ETS, which runs from 2008-12. As a result, the carbon price for 2010 has risen to €16. At the same time, both the commission and the British government are trying to establish a longer-term carbon price. That's the point of Europe's plan to set a binding target of cutting carbon emissions by 20% of their 1990 level by 2020, and Britain's of cutting by 60% by 2050: industry can work backwards from those targets, infer a carbon price and build it into its investment plans. So those targets are not grandiose political gestures but pragmatic attempts to address a practical problem. It's a shame that the same can't be said of Europe's, and indeed America's, approach to subsidies.

Climate change is so wildly fashionable now that hardly anybody dares object to measures designed to combat it. But as the costs of such policies rise, that may not last. The more money governments spend on wasteful subsidies, the bigger the backlash is likely to be, and the smaller the chance of sustaining the political will needed to keep the world cool.

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Microfinance

Time to take the credit

Mar 15th 2007
From The Economist print edition

Aid donors have shown microfinance can work. They should now leave their successes behind

Reuters

SUCCESS has many fathers. No wonder, then, that paternity suits are flying in microfinance—lending small amounts to help the poor pull themselves out of poverty. Thanks first to charities and, later, international financial institutions (IFIs) like the World Bank, microfinance has been shown to work (see article). Now philanthropists such as Bill Gates and Pierre Omidyar, the founder of eBay, are using their own charities to pour money into the field. So, increasingly, is the for-profit sector, including "socially responsible" investors and capitalists more interested in the bottom line than the poverty line.

Microfinance is a promising way to get credit to parts of the economy that are starved of capital. So it is a pity that all these lenders are competing to support the same, small group of microfinance institutions that cater to the most creditworthy borrowers. It would be better for the poor if the IFIs and donors left the best credit risks to profit-seeking lenders and concentrated instead on those still stuck outside the system.

Micromanagement

No doubt that sounds ungrateful. Microfinance is in vogue thanks partly to the IFIs, which provided grants, loans and training to untested microcredit institutions. The private sector shunned the risk—out of ignorance, a lack of expertise and fears that making money from the poor would look predatory. The pioneering work of donors means there are now some 10,000 microfinance institutions lending an average of less than $300 to 40m poor borrowers worldwide.

As a result, microfinance has become profitable. Top-tier microlenders no longer need subsidies or even commercial loans from IFIs or philanthropists. ProCredit, made up of 19 microfinance banks in countries from Moldova to Ecuador, was established in 1998 by some IFIs. Now wildly successful, it boasts over 2.2m customer accounts and arrears by volume of a minuscule 1.2%. So many of its banks make money that it could even list its shares on the stockmarket.

The Inter-American Development Bank has acknowledged that the best microlenders can finance themselves either by gathering deposits to finance loans or by attracting commercial investors. It is busily selling equity stakes in its portfolio of microfinance investments. But other development groups are less willing to cut the apron strings. They continue to devote scarce aid dollars to the microlenders that need them least. Having nurtured these outfits when for-profit groups would not, they now want to bask

in their successes. Some philanthropists, too, prefer to take the safe route and invest in stable, profitable top-tier microfinance groups.

This trophy lending is harmful. By subsidising microfinance groups that do not need it, aid bodies and philanthropists discourage private money, which cannot compete with their soft terms. In the long run, this harms microfinanciers, because it slows their integration into the financial-services industry and thus hampers their transformation into lenders able to stand alone.

Aid money is better spent where commercial cash fears to tread—such as on the next generation of microfinance institutions. Subsidies are often needed to lend to the rural poor, where small, scattered populations make it hard for commercial lenders to cover their costs. Donor funds could be used to invest in technology such as mobile payments, which promise to cut the cost of providing microcredit. Top microfinance institutions themselves may need help in expanding into insurance and other financial products for the poor, as well as in tapping the capital markets. IFIs, in particular, can press foreign governments to get rid of interest-rate caps and other misguided regulations that impede microlending.

Only a fraction of the world's 500m impoverished “micro-entrepreneurs” have access to the financial system. There is not enough donor or “socially responsible” money in the world to meet the demand. That's why microfinance needs private-sector capital. Aid agencies, philanthropists and well-meaning “social” investors can help attract it by investing only where commercial outfits will not. When the children come of age, the best parents step aside.

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On corporate R&D, Guatemala, outdoor activities, generic drugs, Thailand, cricket, Anna Nicole Smith

Mar 15th 2007
From The Economist print edition

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A new blueprint needed

SIR – I read with interest your briefing on the changes that have taken place in corporate R&D since the days of Vannevar Bush, Franklin Roosevelt's science adviser ("Out of the dusty labs", March 3rd). But although you highlighted the flaws in the R&D model employed in the era shortly after the second world war, you neglected the weaknesses of the model that the pendulum has swung towards. For instance, if there are no Bell Labs and Xerox PARCs to perform blue-sky investigative work, how are the frontiers of scientific exploration going to be expanded? Who will develop science that has no immediate application for business?

In America the mix for funding basic research has shifted to one in which industry performs only around 15% of basic research work. We now rely on government to fund our basic research enterprise, largely through universities, yet the latest figures show that federal support for research is about half that of 1985 in constant dollar terms. While the convergence of science and commercial interests is laudable, the erosion of industry support in the pursuit of scientific discovery for its own sake is worrisome.

Burk Kalweit
Alliance for Science and Technology Research in America
Washington, DC

SIR – Basic research, termed "Newtonian research" by Lewis Branscomb of Harvard, and applied research, termed "Baconian research", are not the only options for R&D. Between these two extremes is "Jeffersonian research", where basic research is done with finite societal goals in mind. Vannevar Bush's plans, which laid the foundations of the National Science Foundation (NSF), conceived it would be a Jeffersonian research agency. By the time legislation passed establishing the NSF it had been stripped of pragmatic goals and became in essence a Newtonian agency. In order to utilise Jeffersonian research, the societal goals of research must be defined. This, not the allocation of government funding, is the more difficult question.

Jenn Gustetic
Cambridge, Massachusetts

Why Mr Bush paid a call

SIR – You said that George Bush's visit to Guatemala was "largely to thank the government for joining America's 'coalition of the willing' in Iraq" ("Spring break", March 3rd). In fact, Guatemala was the only country in Central America that did not join the "coalition of the willing" in the absence of a UN Security Council resolution sanctioning the use of force in Iraq.

We would like to think that President Bush's stop in our country was partly because Guatemala has had such a compelling story to tell since the signing of the 1996 peace accords. While still facing difficult challenges, we have made progress towards becoming a pluralist, democratic society. It is well known that the United States has not always been an objective bystander in domestic events, but I am happy to confirm the point you made that in more recent times our bilateral relationship has been very constructive and mutually respectful.

Gert Rosenthal
Foreign minister of Guatemala
Guatemala City

The last boy scouts?

SIR – It is ironic that environmentalists are concerned for the sustainability of their cause because young Americans are spending more time indoors ("No child left inside", February 10th). Greens should take a hard look in the mirror, as much of the blame for this unfortunate trend lies with them. Their agenda is premised on the view that humans are bad for the environment: more wilderness, but no roads for access; trails, but no biking, horses, or camping.

Fishing, a favourite pastime of my youth, is now complicated by numerous regulations, limited seasons and expensive licences. Boating, golfing and skiing lead to interests in other activities (swimming, diving, hiking, etc). But try to build a marina, golf course or ski resort and opposition will come from the greens. Such groups need to realise that responsible and regular use of the outdoors by humans is natural, healthy and good, both for us and the environment.

Bill Youngsman
Shoreline, Washington

Drugs law

SIR – You were inaccurate with respect to America's 180-day exclusivity period for new generic drugs ("Knock it off", February 24th). A generic-drugs firm receives this carrot only if it challenges one or more of the innovator's patents and prevails in court. The law, commonly referred to as Hatch-Waxman, recognises the risks of such litigation and aims to reward generic firms that succeed in lopping years off brand monopolies (ie, manoeuvring against questionable patents that extend these monopolies). If there is no patent challenge, the first firm to win approval for a given new generic is not granted the 180-day exclusivity period.

David Berman
New York

Don't fuel the fire

SIR – The obvious solution to the unrest in southern Thailand may well be to grant the region "special autonomy" ("In need of help to douse the flames", February 17th). Unfortunately this does not augur well for Malaysia, as it would encourage potential separatists in the north of the country to fight for their own autonomous region. An even worse scenario would be if they joined forces with their neighbours to form a new nation. Malaysians can only hope that Thailand's junta will find an amiable solution to contain the insurgence in their restive south in the near future and collaborate with the Malaysian government on questions of citizenship.

Chaan Venn Tzu
Penang, Malaysia

A lack of Wisden

SIR – It is a pity that your otherwise interesting article on the cricket world cup in the West Indies displayed appalling knowledge about the sport ("Beyond a boundary", February 24th). You stated that "the West Indies team is a shadow of the sides that dominated world cricket in the 1960s and, under Sir Vivian [Richards], in the 1970s". That these great sides dominated cricket then (as they would against today's one-day wonders) is not in dispute, but it was mostly "under" Clive Lloyd as captain that they did so. Moreover, the West Indies continued their success in the 1980s, which is when Viv Richards captained the team. I need not mention that you excluded that other great Caribbean, Sir Garfield Sobers, who dominated the cricketing world with grace from the 1950s to the 1970s.

Warren Ganesh
Hong Kong

Legacies

SIR – In response to the letters you received (March 3rd) criticising your choice to run an obituary on Anna Nicole Smith, I would say that part of the joy of reading *The Economist* is to appreciate (for better or worse) how a waitress at Jim's Krispy Fried Chicken in a small Texan town can rise and fall and take a swathe of skilled, educated and talented people along with her.

Nick Jones
Atlanta

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The Chirac legacy

It all went wrong

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Reuters

After 12 years of unkept promises, President Jacques Chirac leaves a confused France longing for someone completely different

Get article background

"OVER the past 20 years, little by little, the French people have divorced themselves from France. An economic crisis seemingly without end has broken for many the link of confidence that tied them to society. There is anxiety over unemployment and the risk of exclusion...Disquiet over a future that casts doubt on a belief inherited from the Enlightenment: that tomorrow will be more glorious than today, and sons happier than their fathers. It is not a matter of fatigue, nor malaise, but a veritable collective depression."

Which of the candidates for next month's two-round French presidential election is this lucid analyst of contemporary France? The answer is: none of them. These were the words of Jacques Chirac, ahead of his election to the presidency in 1995. This was the candidate who promised to "mend the social fracture", get the French back to work, combat racial inequality in the *banlieues*, cut taxes, and put France back on track towards a future of shared prosperity.

On entering the Elysée Palace, Mr Chirac inherited a restive country, with high unemployment, mounting debt, a disoriented electorate and a sense of political stagnation. Twelve years later, having announced his decision not to run again, the 74-year-old Mr Chirac bequeaths to his successor a restive country with high unemployment, mounting debt, a disoriented electorate and an even more intense sense of political stagnation.

During Mr Chirac's two terms in office, French unemployment has averaged 10%, GDP per person has been overtaken by that of both Britain and Ireland, and public debt, at 66% of GDP, has grown faster than in any other European Union country. Over the past two years, the febrile French have rebuffed the president with assiduous regularity. They rebelled over Europe, by saying *non* in a referendum on its proposed constitution in May 2005. The multi-ethnic *banlieues* rebelled over social exclusion in three weeks of rioting in the autumn of 2005. The young rebelled over economic reform by taking to the streets against a less-secure job contract for the under-26s a year ago.

Mr Chirac's popularity rating has slumped from a second-term high of 60% during the Iraq war, according to TNS-Sofres, a polling organisation, to just 29% today. Midway through 2006, he became the most

unpopular president under the French Fifth Republic since polling began.

To the casual visitor to France, a country of high-speed trains, well-stocked municipal flower beds and sit-down lunches, such French glumness is baffling. Fully 54% of respondents told a poll by Ipsos recently that they considered their country to be in decline; only 12% thought the opposite. Underlying this malaise is an intangible sense of insecurity: about finding a regular job; about making ends meet at the end of the month; about the creeping bankruptcy of the social system; about the unresolved tension in the *banlieues*; and about the failure of politicians to make any difference.

Years of unkept promises have undermined trust in the political system. If there was one moment during Mr Chirac's presidency that seemed to capture the gap between the perceptions of ordinary French people and those who govern them, it was a two-hour televised debate held at the presidential palace ahead of the European referendum. Mr Chirac sat on a stool, surrounded by some 80 young people. As the cries of distress and anxiety from the audience multiplied, Mr Chirac's brow creased. “I'm going to tell you,” he said, “very frankly, I don't understand it.”

All these troubles cannot be laid at the door of Mr Chirac alone. In his first years in office, in an effort to curb public spending, he did appoint a reformist government, under Alain Juppé. But his attempts to push through bold welfare reform were defeated by strikes and demonstrations. After a disastrous decision to dissolve parliament in a bid to seek a mandate for reform, Mr Chirac then lost his majority and spent five years “cohabiting” with a Socialist-led government, which brought in the 35-hour working week, the source of so much consequent upheaval.

All the same, Mr Chirac, the only serving politician who has belonged to governments under every Fifth Republic president since Charles de Gaulle, deserves his full share of the blame. He had the chance to make a difference. In his second term, he was elected with 82% of the vote, after the shock appearance of the far-right Jean-Marie Le Pen in the run-off, and backed that up with a handsome parliamentary majority. Yet he has come to embody the non-confrontational, risk-averse approach to governing the country that, in many ways, has characterised French political leadership for the past quarter of a century. This manner of government is neither clearly to the right, nor to the left; it shies away from conflict, and it denies the depth of the underlying problem.

Over a 40-year career in national politics, Mr Chirac has mocked political classification. Descendant of Gaullism, he was the dynamic two-time prime minister (1974-76 and 1986-88) who, in his liberal second spell, demolished the Socialist programme of the early 1980s, carrying out extensive privatisation and abolishing the wealth tax. Yet, as president, Mr Chirac has compared the dangers of liberalism to those of communism, increased the state's overall tax take and defended the strained French social system as “perfectly adapted” to the modern era.

As a student, Mr Chirac spent a summer at Harvard, worked in a Boston fast-food joint and hitch-hiked across America. Yet, as president, he has advocated a “multi-polar world” to counter American power, and, over Iraq, managed the worst fallout with an American president for some 40 years. Mr Chirac conducted nuclear tests, yet converted to ecology; courted African leaders, yet defended French farming subsidies; promoted Europe, yet failed to campaign vigorously for its first constitution. In practice, the Gaullist Mr Chirac has governed as a politician of the anti-liberal left, or what the French know as a “rad-soc”: radical socialist.

A question of principle

Despite this zigzagging political trajectory, Mr Chirac has taken commendable stands on certain matters. He was the first French president to recognise the official responsibility of the French state for the deportation of Jews from Vichy France under Nazi occupation. He has made a point of trying to stamp out anti-Semitism and racist extremism, refusing a decade ago to let his party enter political pacts with the National Front in order to hang on to power in the regions. This week, in his televised retirement declaration, he repeated his message: “Never compromise with extremism, racism, anti-Semitism or the rejection of the other. In our history, extremism has already almost led us into the abyss.”

Mr Chirac's long-standing fascination with non-Western cultures—he collects Asian and African artefacts, and set up a new Paris museum devoted to this theme—as well as his fear of a clash of civilisations, has made him a champion of Turkish entry into the EU, despite the hostility of his fellow countrymen. On Iraq too, there may be lingering American suspicions about the Arabist Mr Chirac's motives for opposing the war, and the way he did it was heavy-handed. Yet even his detractors cannot deny that Mr Chirac's analysis of the risks of that war turned out to be prescient.

At home, Mr Chirac's political career has been marked less by ideological coherence, or even by an evolution in thinking about the use of power, than by a relentless thirst to win it. He has been a master of political opportunism. For the presidential election in 1974, he ditched a Gaullist resistance hero, Jacques Chaban-Delmas, to back the rising star of the centre-right, Valéry Giscard d'Estaing, who went on to win. According to Mr Giscard d'Estaing's recent memoirs, Mr Chirac then swung against him in 1981 and secretly backed François Mitterrand, whom he wrongly imagined would not last.

Genuine warmth and a flair for pressing the flesh have made Mr Chirac a formidable campaigner. For 30 consecutive years, since his first election as mayor of Paris, he has lived in state palaces, swapping periods in the prime minister's mansion for spells back across the Seine in the town hall. Indeed, it was during his time as mayor of Paris that the party-financing scandals took place which led in 2004 to the conviction for political corruption of Mr Juppé, Mr Chirac's right-hand man. Mr Chirac's departure from the Elysée in May will end his presidential immunity, over this affair as well as any other judicial investigation that might arise.

Down with change

Mr Chirac appears to have concluded that the French are too conservative to accept change. This, at any rate, is how the centre-right presidential candidate for his UMP party, Nicolas Sarkozy, sees it, however self-servingly. “He thinks France is fragile and resistant to change,” Mr Sarkozy wrote of Mr Chirac in a recent book: “I think France is impatient, exasperated by delays, and eager for profound change.”

Mr Chirac also seems to have concluded that—despite his 1995 campaign theme—not much in France needs to be changed. This week he again insisted that “our French model” must never be dismantled. He has vehemently rejected the idea that the country has anything to learn from a place like Britain, whose unemployment rate is 5.5% next to 8.6% in France, because its laissez-faire social rules would “never be accepted or acceptable for us.”

It is true that parts of the dirigiste French model, of high taxes and high spending by a strong state, do indeed work well. They have delivered the country efficient public transport, nuclear energy and first-rate health care. Yet the model is not only unsustainably expensive but fundamentally weakened by its failure to reduce unemployment. The jobless rate has not dipped below 8% for 25 years, despite spending on subsidised jobs. The figure reaches 21.5% for the under-25s, and close to 50% on the housing projects of some *banlieues*. Since tight job protection now deters job creation, young people spend years temping, or on short-term contracts, undermining the concept of protection that the system is supposed to guarantee.

AFP

Paris cheers its triumphant mayor

At the same time, the burden of regulation has stifled innovation and growth, and the hefty cost of administering it is piling up debt for future generations. Over the past 20 years, a million extra civil servants have been recruited. Despite mini-reforms of pensions and health care on Mr Chirac's watch, the social-security deficit is heading for more than €1 billion ($1.3 billion) by 2009, say official estimates.

France's failure to face up to these shortcomings during the Chirac presidency contrasts with Germany, which has passed reforms and where business has made a huge effort to regain lost competitiveness. Whereas Germany was for years the biggest drag on the euro area's growth, that honour is now being transferred to France. Beneath the glossy veneer of France's world-class commercial giants—L'Oréal, Michelin, Total, Carrefour—which last year reaped record profits, the broad French corporate middle is failing to benefit from the expansion of global trade. Between 1999 and 2006, the share of French exports outside the euro area dropped by 18%, while Germany's share grew by 15%. With GDP growth of 2% last year, next to 2.6% in Germany and a euro-zone average of 2.8%, France, according to Eric Chaney, chief economist for Europe at Morgan Stanley, is “the new sick man of Europe”.

Disowning the president

It is a mark of the mismanagement of the past 12 years that each of the three leading candidates to succeed Mr Chirac—Mr Sarkozy on the right, Ségolène Royal on the left, and François Bayrou in the

centre—is, in their own way, standing on an anti-Chirac platform. That the Socialists' Ms Royal should seek to turn the page on the Chirac years is scarcely surprising. That the two other mainstream candidates do too testifies to the depths of public disillusion with their outgoing president.

The first oddity of this election is that Mr Chirac has no natural successor from his own political family. On paper, it appears to be Mr Sarkozy. But Mr Chirac has not yet endorsed his candidacy. One by one, he has tried, and failed, to nurture alternative successors on the Gaullist right. Mr Juppé, his chosen heir, was disqualified by his conviction. Dominique de Villepin, the prime minister, who publicly backed Mr Sarkozy's candidacy this week, ruled himself out by mismanaging the mass strikes and student protests last year.

AFP

Little-guy Bayrou (centre) threatens the big guys, Sarkozy and Royal

As it has turned out, the man representing the president's Gaullist party is in reality running on a right-wing programme that blends elements of economic liberalism with social authoritarianism in a way that sets him quite apart from Mr Chirac. Given the president's unpopularity, this may be a wise electoral strategy. Mr Sarkozy still tops the polls in the first round, but his lead has been narrowing rapidly. With five weeks to go before the first round of voting, on April 22nd, the presidential race is turning out to be wide open. Latest polls show the three leading candidates tightly bunched: Mr Sarkozy with 27%, Ms Royal with 26%, and Mr Bayrou with 23%.

The second unexpected feature of this campaign is the spectacular recent surge in the polls of Mr Bayrou, leader of the Union for French Democracy (UDF), a minority parliamentary party. Once education minister, he is a horse-breeder from the south-west who likes to be photographed driving his tractor and has carefully cultivated an anti-elite image. In little over a month, he has doubled his poll numbers and established himself as a genuine threat. If Mr Bayrou were to make it through to the run-off, according to a poll by Ifop, he would beat both Ms Royal, by 57% to 39%, and Mr Sarkozy, by 59% to 40%.

This would be a breathtaking upset for the two hitherto-leading candidates. What explains Mr Bayrou's late and unexpected emergence? Partly, it is to do with Ms Royal's troubles. She has struggled—against, she insists, macho French culture—to appear competent, but has made a string of foreign-policy gaffes. This was followed by an old-style high-spending electoral programme that was long on crowd-pleasing ideas but short on how to finance them. She has battled to impose her authority on the Socialist Party heavyweights, trying first to conduct the campaign without them, and now fighting to keep them on board.

Mr Bayrou has also taken advantage of Mr Sarkozy's right-wing positioning. Having won support from the Socialists, the centrist is now making inroads into the centre-right, among those turned off by Mr Sarkozy's hard talk. A tough-minded interior minister who has courted the right-wing vote with a firm line on crime, immigration and questions of national identity, and promised to overhaul the French social model, Mr Sarkozy had begun to temper such radical talk with softer messages designed to soothe and reassure the centre. Yet he may have left this shift too late to squeeze out Mr Bayrou.

Mr Bayrou seems to have tapped into the popular dissatisfaction with mainstream politicians that has spread during the Chirac years. He has a simple message: a promise to “govern beyond the left-right divide”, and a short programme that chiefly promises not to spend what France cannot afford. He seems to be on to something. A poll this week suggested that 61% of the French had no confidence in either the left or the right.

Although Mr Bayrou has long been a familiar figure in France, and has no particular political achievement

to speak of, he is promoting himself as the outsider, the little guy, crushed by the big campaign machines. This week, he studiously headed off to campaign in the Paris *banlieues* in an overcrowded public RER train. To the popular cry, “They are all the same”, Mr Bayrou seems to be claiming: “Except me!”

How he would ever manage to run a stable government is another matter. His UDF, the descendant of Mr Giscard d'Estaing's centre-right party, currently has just 27 seats in parliament out of 577, compared with the 359 for Mr Chirac's UMP. Legislative elections are due in France in May and June. Short of a massive increase in parliamentary seats, a victorious Mr Bayrou could hope to govern only in a formal coalition or by drawing deputies from today's two big parties. In either case, it hardly looks like a recipe for the stable government and authoritative policymaking that France so desperately needs.

Electoral insurgency

In short, as Mr Chirac reaches for his slippers, it is wholly uncertain to whom he will hand over the palace keys. The possibility that it will be Mr Bayrou rather than Mr Sarkozy or Ms Royal cannot be firmly ruled out. The pesky, dissatisfied French, after all, are specialists at staging electoral insurgencies. They voted Mr Le Pen into the second round in 2002; and the far-right leader confirmed this week that he has the required 500 signatures he needs to appear on the ballot this year too. The French rejection of the European constitution was also a revolt by the ballot box. Indeed, since 1981 they have never re-elected an incumbent government.

The French seem to love a poll upset. Back in 1995, it was the last-minute surge in the closing weeks by a certain Jacques Chirac that deprived the establishment favourite, Edouard Balladur, of victory. But had President Chirac spent the following 12 years reviving the French economy and modernising the welfare state, the country might not now be yearning so keenly for someone different.

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George Bush, Congress and the law

Three clashing branches

Mar 15th 2007
From The Economist print edition

Getty Images

A kerfuffle over sacked prosecutors riles the White House

BEFORE last year's election, Nancy Pelosi, now the speaker of the House of Representatives, enthused to the *New Yorker* about one particular consequence of a Democratic victory. “We win in '06, we get subpoena power,” she said. Her interviewer observed that she “appeared excited by the prospect”. No wonder. Control Congress, and you can order probes into anything the White House has done that you deem fishy. This week's scandal concerns eight United States attorneys whom the Justice Department sacked last year.

Some of these attorneys say they were booted out for political reasons. One had refused to pursue allegations of voter fraud in the 2004 governor's race in Washington state, which a Democrat won by a hair's breadth. One successfully prosecuted a former Republican representative for conspiracy. Another complained that he felt pressure from a Republican senator, Pete Domenici, who called him at home to ask whether indictments in a corruption case involving state Democrats would be handed down before last year's elections. And one in Arkansas was pushed aside to make room for a chum of Karl Rove, George Bush's top strategist.

To make matters worse, the White House at first failed to admit to its own role in the firings. Alberto Gonzales, the attorney-general, suggested that all eight were dismissed for poor performance, though most had received warm reviews. Charles Schumer, a Democratic senator from New York, called the firings an “unprecedented breach of trust, abuse of power and misuse of the Justice Department”. Hillary Clinton and John Edwards, two Democrats with ambitions, called for Mr Gonzales to resign. Other Democrats called for Mr Rove and Harriet Miers, the president's former counsel, to testify before Congress. On March 14th John Sununu, a senator from New Hampshire, became the first Republican to say that Mr Gonzales should go.

The issue is cloudier than partisans acknowledge. US attorneys, who represent the federal government in district courts, serve at the president's pleasure. He appoints them. He can fire them. Ronald Reagan and Bill Clinton, on taking office, each replaced all 93 US attorneys with ones they preferred. Mr Bush did the same. And a little-noticed aside in the Patriot Act of 2001 has allowed his attorney-general to appoint US attorneys indefinitely on an “interim” basis without Senate approval, though Mr Gonzales has agreed to yield this power.

Regarding the current cases, Stuart Taylor, a writer on legal affairs for the non-partisan *National Journal*, argues that it is reasonable for a president to dismiss a prosecutor over policy (for example, if the White House favours the death penalty and a prosecutor never seeks it), but not for partisan reasons. The voter-fraud cases are a difficult call. Republicans are convinced that pro-Democrat groups often inflate voter rolls by helping to register aliens, felons and underage citizens, who they assume will vote Democratic. Democrats are equally convinced that Republican efforts to curb voter fraud are designed to disenfranchise two of their core constituencies, the poor and the non-white.

A sheaf of internal e-mails handed over by the administration and distributed by House Democrats this week provided ammunition for the Democrats. Two years ago, Ms Miers floated the idea of firing all 93 US attorneys. Mr Gonzales dismissed this as impractical. Kyle Sampson, his chief of staff, suggested that they remove a handful of attorneys “who have been ineffectual managers and prosecutors, chafed against administration initiatives, etc”, while leaving in place those who have “produced, managed well and exhibited loyalty to the president.”

Democrats seized on the words “loyalty to the president”: an attorney's foremost duty is to the law, not his boss's boss. Mr Sampson, who came up with the unfortunate phrase, resigned on March 12th. Nonetheless, some of the administration's complaints about the soon-to-be sacked attorneys sound substantial. One was apparently loth to pursue illegal-immigration cases. Another refused to toe the line on the death penalty. And the voting-fraud cases involved credible evidence.

For Mr Bush's critics, both Republicans and Democrats, this tale reinforces two conclusions they drew some time ago. First, Mr Bush is asserting greater executive power, at the expense of other branches of government, than any previous chief executive. And second, the president is too fond of mediocre loyalists such as Mr Gonzales. That said, if he sacks him, he will have a heck of a job getting a replacement confirmed by the Senate.

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Campaigning on the internet

Of slips and video clips

Mar 15th 2007 | WASHINGTON, DC
From The Economist print edition

Candidates for 2008 are racing to master a new medium

DURING the presidential campaign of 1800, partisans harnessed high-speed technology to spread their message. Like today, that message was often scurrilous. Unlike today, the technology they harnessed needed real harnesses. When Thomas Jefferson's enemies wanted to distribute pamphlets accusing him of atheism and adultery, or to spread a premature report of his death, they used horses, which could outrun even the most rapid rebuttal.

Candidates for the presidency in 2008 have a wider range of media through which to spread dirty but memorable sound-bites, or even to discuss the issues. On their websites, all the serious candidates have posted footage of themselves endeavouring to sound presidential yet approachable.

At HillaryClinton.com, for example, you can watch a “Hillcast” in which the junior senator from New York calls for “a new GI Bill of Rights” so that wounded American troops are treated less bureaucratically. If you find the message inspiring, you can join like-minded people discussing it at blogHillary, her campaign blog. (“Another wonderful speech,” gushes a typical supporter; another advises Mrs Clinton to work on her body language.) Then you can join the “Hillraisers” who are busy raising money, or find a Hillary-supporting event happening near your home, or download the necessary tools to organise one yourself.

From a candidate's point of view, the great advantage of the internet is that you can send a lot of information to a lot of people at minimal cost. The downside is: so can your opponents and anyone else with a keyboard or a camera phone.

Go to YouTube.com, a free website for sharing video clips, and the most popular Hillary-related items are unflattering. Over 1m people have watched and heard her caught on an open microphone singing the national anthem out of tune. Many others have browsed snippets with titles such as “Hillary goes nuts”. And someone called “ParkRidge47” has posted a stylish but nasty video showing Mrs Clinton as a dictator addressing brainwashed peons in drab uniforms. The video then urges viewers to support Barack Obama so that 2008 won't be like 1984.

Who is “ParkRidge47”? “It could have been anybody,” says Carol Darr, director of the Institute for Politics, Democracy and the Internet at George Washington University. And that is a sign of things to come. Whereas people used to put anonymous fliers under windscreen-wipers at malls, now anyone can mount an anonymous attack nationwide. Of course, it has to be attention-grabbing to “go viral”—ie, for everyone who sees it to link to it on their blogs or e-mail it to their friends. “It will be the meanest, snarkiest and funniest stuff that will get an audience,” says Ms Darr. And lots of people are working on it.

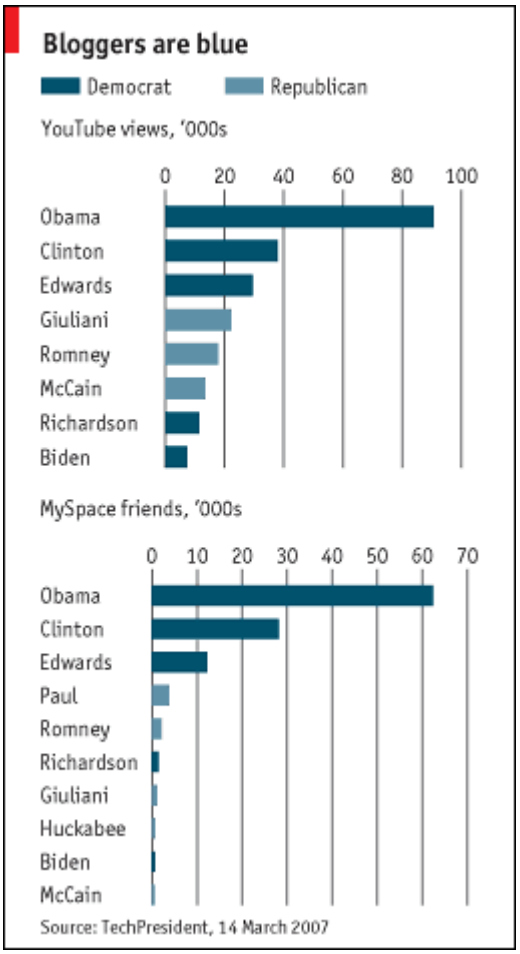
Video clips are a good way of making candidates look two-faced. Opponents of Mitt Romney, a Republican who stresses his belief that abortion and gay marriage should be banned, have dug up footage from a Senate race in Massachusetts in 1994 in which he said the opposite. Mr Romney says his change of heart is sincere, not opportunistic. But potential supporters, watching him declare that “you will not see me wavering” from positions he has since abandoned, may waver.

Critics of John McCain, another leading Republican, have posted clips of him saying contradictory things about Iraq, gay marriage and the preacher Jerry Falwell, whom he once called an “agent of intolerance” but now courts. An honourable man can change his mind, but when you compress each flip into a few seconds and add shots of Mr McCain promising always to tell the truth, the result is armour-piercing.

To use the internet effectively, candidates need to create “communities”, argues Joe Trippi, a former adviser to Howard Dean, a Democrat whose web-based campaign briefly soared in 2004. It is not enough

just to have a blog where the candidate lays out his views. Supporters must be inspired to write their own blogs, talk to each other and devise their own ways of raising money. The candidate who does this best could raise half a billion dollars, says Mr Trippi.

So far, the most effective candidate on the web has been Mr Obama. More than twice as many people watch videos about him on YouTube as his nearest Democratic rival, Mrs Clinton, and four times as many as the top Republican, Rudy Giuliani (see chart, above). On social networking sites popular with young people, such as Facebook and MySpace, he reigns. As of March 14th, 62,801 people had signed up as his “friends” on MySpace. Mrs Clinton had barely half as many cyberpals, while the Republicans were nowhere. Their most popular candidate, by this measure, was Ron Paul, an obscure outsider from somewhere in Texas.



John Edwards, a populist Democrat, is also doing well. His website has all the details of his plan for a national health-care system. His campaign blog is quick to jump on the latest Republican outrages, and has lively chats between people who say things like: “Can anyone view this photo of John Edwards...and not see his compassion, and yes, even love, for the elderly woman to whom he is speaking?” But he, too, has found that he cannot always control the message. He hired two professional bloggers, only to discover that they liked foul language and despised the Catholic Church. (In the ensuing hoo-hah, they resigned.) And for all but the most ardent fans, the enduring image of Mr Edwards from this campaign is one of him spending a full two minutes primping his hair before a television interview, posted on YouTube to the tune of “I Feel Pretty”.

How important is all this? Mr Trippi thinks the internet will have “an explosive impact” on the campaign. It will allow candidates to reach young voters, who are growing less apathetic about politics. It will allow the most committed (and extreme) activists to organise themselves, with minimal guidance from the candidate they support. It may also coarsen the tone of political debate, worries Stuart Rothenberg, a political analyst. Bloggers, especially lefty ones, use swear-words the mainstream media shun.

But steady on, says Larry Sabato, a political scientist at the University of Virginia. “The occasional hot YouTube video will be seen by one or two million people, but these are people who are already getting political information from 10-20 sources every day,” he says. “The essence of politics has not been transformed. It's still about whether people like your candidate and believe his [message].” Plus, there is still nearly a year to go before the primaries. That is a long time in politics and an eternity on the internet.

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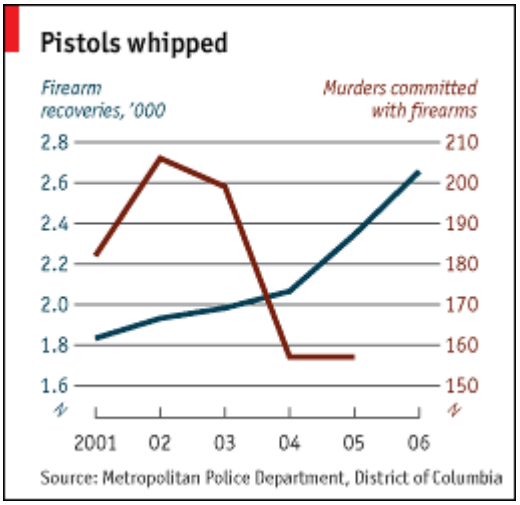
Gun control

One step back

Mar 15th 2007 | WASHINGTON, DC
From The Economist print edition

Washingtonians are allowed to keep and bear arms



ON MARCH 9th the US Court of Appeals for the DC Circuit overturned the District of Columbia's long-standing ban on handguns. Some might say, so what? Last year the police recovered 2,655 guns in the District, which hardly suggests that the ban was keeping guns out of circulation. Nonetheless, Washington, DC, has long been a small spot of resistance to a culture all too tolerant of firearms.

In a 2-1 decision, the judges rejected the District's claim that the Second Amendment applies only to militias. The rights protected in the amendment "are not limited to militia service", the majority argued, "nor is an individual's enjoyment of the right contingent upon...enrolment in the militia".

The debate about the meaning of the second amendment is one of the fiercest in constitutional law. In 1939 the Supreme Court ruled, in *United States v Miller*, that the amendment was adopted "with [the] obvious purpose" of protecting the ability of states to organise militias, and "must be interpreted and applied with that end in view". More recently, the individual-rights view has been gathering support, and not just from the Bush administration and the National Rifle Association (NRA).

In 2001 the US Court of Appeals for the Fifth Circuit (which includes gun-loving Louisiana, Mississippi and Texas) embraced the individual-rights view. The DC lawsuit was filed in 2003, nine months after the then attorney-general, John Ashcroft, argued that individual gun bans are unconstitutional. If the District appeals the ruling, as Mayor Adrian Fenty says it will, there is a good chance that the Supreme Court, with its conservative majority, will come down on the side of individual rights.

The Court of Appeals decision is just the latest in an almost unbroken series of advances for the gun-rights lobby. The NRA has made a steady progress in loosening local gun controls, particularly in pushing "concealed carry" laws, which now exist in 48 states. The Democrats have softened their anti-gun stance in an attempt to make advances in "red America"—particularly in the all-important mountain West where gun rights are sacrosanct and the next presidential election may be decided. Brian Schweitzer, the Democratic governor of Montana, speaks for a new breed of pro-gun Democrats when he says that he has "more guns than I need but not as many as I want".

A few clouds loom on the horizon for gun-rights supporters. On the very day of the DC ruling the Police Executive Research Forum, a police think-tank, reported that violent crime, including homicides, had been rising rapidly since 2004. Meanwhile, the NRA is slowly losing one of its most important constituencies: the proportion of Americans holding hunting licences has declined from 10% in 1985 to 6% last year. If both trends continue, more and more Americans will come to associate guns not with healthy outdoorsmanship, as the NRA would like, but with swift and violent human death.

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Presidential libraries

A room of his own

Mar 15th 2007 | AUSTIN
From The Economist print edition

George Bush wants his library to propound his message

THE race is now decided. Southern Methodist University (SMU) in Dallas will enjoy the dubious honour of being host to George Bush's library. From Mr Bush's perspective, it was an easy choice: after all, Laura Bush is an alumna and trustee. Wealthy donors in Dallas will be happier to contribute million-dollar cheques if the money is staying in town rather than flowing down the road to Baylor University in Waco, another of the finalists. And Mr Bush's library will be easier to visit than his father's, which is hidden away at Texas A&M University in College Station.

It may seem like a coup for the university, too. Housing the George W. Bush presidential library and museum will bring SMU money and attention. But Mr Bush's plans for managing his legacy have ignited a fierce debate about what SMU may have to sacrifice in return. The president hopes to raise $500m for the project. This would make it the most expensive presidential library ever, $335m more costly than Bill Clinton's in Little Rock. For Mr Bush wants to build, alongside the library and museum, an institute devoted to promoting his policies and ideas.

Some members of the faculty think this a bit dodgy. In an op-ed article in the *Daily Campus* last November, two professors at SMU's Perkins School of Theology wondered bitterly whether housing the library would force the school into a queasy alliance with “a legacy of massive violence, destruction, and death brought about by the Bush presidency.”

It may; but the more problematic issue is whether the planned Bush Institute will infringe SMU's academic freedom. The university could end up with no supervision of a strongly partisan body. At worst, the Bush Foundation could be free to staff the institute with pseudo-scholars happily lavishing praise on Mr Bush under SMU's aegis.

It is also unclear whether the library will be able to make Mr Bush's papers available to genuine scholars and historians. This has been a key purpose of presidential libraries since Franklin Roosevelt built the first one. Roosevelt made his papers public of his own volition, but more recent presidents have not had a choice in the matter. The 1978 Presidential Records Act, passed in the wake of Watergate, made presidential papers public property. In 2001 Mr Bush issued an order allowing him radically to restrict access to his documents for years after he leaves office; on March 14th the House of Representatives passed a bill that nullified that order. Debate may continue.

Plans for a George Bush library were bound to be dogged by jokes about the president's literacy. Get a Bible and a beanbag and call it a day, you might say. But presidential libraries typically handle their subjects with generous and appealing detail. The Lyndon B. Johnson Library and Museum at the University of Texas at Austin features an animatronic Johnson who leans on a fencepost and tells stories. The Hoover Library covers “Hoover-ball”, a tennis-volleyball hybrid that Herbert Hoover played with staff and cabinet members on the White House lawn each morning. Mr Bush's library may perhaps feature the comfort pillow he likes to take on all his travels, together with plush models of Barney and Miss Beazley, the president's Scottish terriers.

But whether the Bush Institute buzzes with interest, or sits mournfully empty, will depend on how Mr Bush is seen by history. And he himself, for all the self-aggrandisement, has also scoffed at the notion that a president should worry about his legacy. In the long run, as he once sagely said, “We'll all be dead.”

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New Orleans's slow recovery

The long road home

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As time goes by, Louisiana's flood victims wait, and wait

AP

A FEW months ago, opponents of Kathleen Blanco (pictured) were grumbling that it was unfair of the governor to have included her own name in Louisiana's nascent homeowner-aid programme for Katrina victims. Tens of thousands of voters, they said, would be receiving cheques from Ms Blanco's office at the very moment that her re-election campaign got under way. Their gratitude would sweep the Democratic incumbent to victory.

The grousing turned to malicious laughter as “Governor Blanco's Road Home Programme” became a synonym for official ineptitude. The programme, which has been in operation since late last summer, offers owners of flood-damaged homes up to $150,000 in aid, depending on the circumstances. Although there was a spurt late last month, so far less than 3% of the 115,000 families who have applied for help have reached “closing”: that is, surmounted the sclerotic programme's various bureaucratic hurdles and received money in the form of buy-out cheques or repair payments.

The lethargic pace has been ruinous for New Orleans and its hard-hit suburbs. In the city, the lack of financial help, combined with Mayor Ray Nagin's loyalty to market forces, have left people whose houses were destroyed or damaged in a kind of purgatory. The market has yet to take shape, since so many people are still waiting for their money. Many sections of town look as lifeless as they did after the floods in September 2005.

Critics point out that in neighbouring Mississippi, 89% of the 14,623 applicants deemed to qualify for homeowner aid have reached “closing”, and 78% have received their cheques. While it took Congress nearly a year to approve the $10.4 billion that is the basis of Louisiana's programme, Mississippi, with a far more powerful congressional delegation, got its federal money months earlier.

Ms Blanco's reputation has suffered accordingly: her approval rating is now much the same as George Bush's. A recent poll showed her getting trounced by Bobby Jindal, a Republican congressman from the New Orleans suburbs, who lost to her in a narrow race in 2003 and who has already declared his candidacy this year.

To what extent is Ms Blanco really responsible for the mess? The programme is run by ICF International, a company selected for the job by her administration after an open procurement process. Although ICF has few obvious connections to Louisiana politics, the terms of the deal raised eyebrows: the company

stands to earn $756m from the job, about $1 for every $9 it doles out. The governor has tried to hold the lagging company's feet to the fire, but to little effect. In December the state legislature asked her to sack ICF, but she demurred, saying that to start all over again with a new firm would just set things back further.

Congress was certainly slow in approving the money, but Ms Blanco was no less slow in laying the groundwork—which should have been ready when the federal cash at last arrived. In the days when the programme was being designed, some observers, including Mr Nagin, argued that setting up a new bureaucracy from scratch was a mistake. He and others proposed that Road Home should use bankers, mortgage-brokers and other existing institutions to disburse the money. Ms Blanco disagreed, but those comments now look prescient.

Possibly the programme may at long last be hitting its stride. But this poses another big problem: can the state's construction industry keep pace with the huge number of jobs with which it will soon be confronted? The answer is almost certainly no. Tens of thousands of New Orleanians remain in trailers, and a good number of them can expect to be there for a long while yet.

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Civil confinement

Locked up, just in case

Mar 15th 2007 | NEW YORK
From The Economist print edition

New York strengthens its sexual-predator laws

POLITICIANS like to do their best to protect their constituents from rape and murder. Statistics show that sex offenders have high rates of recidivism. So legislation to protect people from sex offenders, even when they have served their time, is highly popular. Megan's Law, passed at state and federal level more than a decade ago, requires public notification when a released sex offender moves into a neighbourhood. Jessica's Law requires some convicted sex offenders to wear GPS devices for five to ten years. It is no accident that these laws are named after victims.

New York is about to go even further. Eliot Spitzer, the state's steamrolling governor, signed legislation on March 14th authorising “civil confinement” of certain sex offenders who have finished their prison terms and are still considered a threat. Nineteen states have some form of civil confinement, and the Supreme Court has upheld states' rights in this matter. William Rehnquist, the previous chief justice, once asked, “What's the state supposed to do, just wait till he goes out and does it again?” President George Bush has earmarked funds to states that keep sex offenders locked up after their sentence ends. The Justice Department is considering civil confinement as well.

Not everyone is a fan. Eric Janus of William Mitchell College of Law, the author of “Failure to Protect: America's Sexual Laws and the Rise of the Preventive State” (Cornell University Press), thinks civil confinement is “a mistake” and that funds could be better directed. Other critics say that confinement means poor surveillance and costly upkeep, with little evidence that the treatment even works.

Yet Mr Spitzer vows that New York's system will be a national model. Under the bill's provisions, a panel made up of mental-health experts will evaluate each case. The state attorney-general will then determine whether to go to court. A jury must unanimously agree that confinement is necessary, and finally a judge must rule on the matter. The presumptive offenders will stay in highly secure psychiatric facilities, segregated from other patients; Mr Spitzer has proposed converting a prison. An Office of Sex Offender Management will be set up to oversee it all.

The new bill makes treatment mandatory both during incarceration and after release; imposes longer prison terms for sex crimes; and demands longer periods of parole supervision for those not confined. It also sets up a new crime of sexually motivated felony. About 1,500 inmates could be subject to civil confinement, but only a few hundred are likely to be kept locked up. The cost of confinement will be about $80m a year—much more than prison.

Meanwhile, Ohio lawmakers want to issue bright-green licence plates for sex offenders' cars (a pink proposal, in 2005, was unsuccessful). New Jersey is considering prohibiting released sex offenders from using the internet. In Texas, a proposed bill calls for the death penalty for repeat sex offences against victims under 14. Much more disturbing, however, not least because it is much more popular, is the policy of locking up people for crimes they might commit.

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Drunk driving in New Mexico

Steady on the tequila

Mar 15th 2007 | ALONG HIGHWAY 285
From The Economist print edition

Of talking urinals and stalled cars

IT IS best not to drive in New Mexico after sundown, or so one infers from the road signs. Divided highways in rural areas are peppered with “Wrong Way” and “Do Not Enter” warnings, implying that drivers stumbling out of bars have a habit of turning into oncoming traffic. Other signs show photographs of drunk-driving victims.

New Mexico has the seventh-worst drunk-driving rate in the country, with 189 people killed in alcohol-related accidents in 2005, a drop of 11% from the previous year. Montana's alcohol crash-rate is by far the worst; the safest state is Utah, whose Mormons avoid saloons.

In 2004 New Mexico's governor, Bill Richardson, his eye then as now on the presidency, created the post of DWI (driving-while-intoxicated) tsar, and his state is taking ever more creative measures to combat the scourge. Last week lawmakers passed a bill penalising drivers who come to New Mexico with drunk-driving convictions from other states. They must now install devices in their cars that prevent them starting if alcoholic breath is detected. The law was prompted in part by the deaths last autumn of a Las Vegas family of five, who collided with a drunk driver heading the wrong way on a New Mexico interstate.

Then there are the talking urinals. Earlier this year New Mexico set up 500 of these in bars and restaurants. “Hey, big guy. Having a few drinks?” asks a woman's voice as her captive audience gets ready to pee. “Think you had one too many? Then it's time to call a cab or call a sober friend for a ride home.” The devices, hidden in deodorising blocks, cost $21 and last three months. Whether they work, or just drive people to drink, remains to be seen.

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Lexington

Taming Leviathan

Mar 15th 2007
From The Economist print edition

Kevin Kallaugher

These are both the best of times and the worst of times for the American-Jewish lobby

THIS week saw yet another reminder of the awesome power of “the lobby”. The American Israel Public Affairs Committee (AIPAC) brought more than 6,000 activists to Washington for its annual policy conference. And they proceeded to live up to their critics' darkest fears.

They heard from the four most powerful people on Capitol Hill—Nancy Pelosi and John Boehner from the House, Harry Reid and Mitch McConnell from the Senate—as well as the vice-president (who called his talk “The United States and Israel: United We Stand”) and sundry other power-brokers. Several first-division presidential candidates held receptions.

The display of muscle was almost equalled by the display of unnerving efficiency. There were booths for “congressional check-in”, booths for “delegate banquet troubleshooting”, and booths full of helpful young people. The only discordant note was sounded by a group of a dozen protesters—Orthodox Jews in beards, side-curls and heavy black coats—holding up signs saying “Stop AIPAC”, “Torah forbids Jews dictating foreign policy”, and “Judaism rejects the state of Israel”.

The lobbyists had every reason to feel proud of their work. Congress has more Jewish members than ever before: 30 in the House and a remarkable 13 in the Senate. (There are now more Jews in Congress than Episcopalians.) Both parties are competing with each other to be the “soundest” on Israel. About two-thirds of Americans hold a favourable view of the place.

Yet they have reason to feel a bit nervous, too. The Iraq debacle has produced a fierce backlash against pro-war hawks, of which AIPAC was certainly one. It has also encouraged serious people to ask awkward questions about America's alliance with Israel. And a growing number of people want to push against AIPAC. One pressure group, the Council for the National Interest—run by two retired congressmen, Paul Findley, a Republican, and James Abourezk, a Democrat—even bills itself as the anti-AIPAC. The Leviathan may be mightier than ever, but there are more and more Captain Ahabs trying to get their harpoons in.

Some of the most determined are Arab-Americans, who have been growing in numbers and influence for years—there are probably about 3.5m of them—and who have been in the eye of a political storm since September 11th 2001. They are a growing political force in northern Ohio and Michigan, and their

institutions, such as the Arab American Institute and the Council on American-Islamic Relations (CAIR), have plenty of access to Middle Eastern money.

But so far their performance has been unimpressive. James Zogby has been promising a breakthrough for his Arab American Institute for 20 years. CAIR remains marginal. Arab-Americans are badly split between Christians (63%) and Muslims (24%). They have also been late in taking to politics. Between 1990 and 2004 Arab-Americans donated $788,968 to candidates and parties, compared with $56.8m from pro-Israeli groups.

AIPAC's ace in the hole is the idea that it represents Jewish interests in a country that is generally philo-Semitic. But liberal Jewish groups retort that it represents only a sliver of Jewish opinion. A number of more liberal groups have started to use their political muscle—groups such as the Religious Action Centre of Reform Judaism, Americans for Peace Now and the Israel Policy Forum. These groups scored a significant victory over AIPAC by persuading Congress to water down a particularly uncompromising bit of legislation, the Palestinian Anti-terrorism Act, which would have prevented any American contact with the Palestinian leadership. This accomplishment led to a flurry of speculation that George Soros might try to institutionalise this successful alliance by creating a liberal version of AIPAC.

It has yet to materialise. And it is doubtful whether Mr Soros, a left-wing Democrat who has little sympathy with Israel, would be the best patron for such an organisation. But the growing activism of liberal Jewish groups underlines a worrying fact for AIPAC: most Jews are fairly left-wing. Fully 77% of them think that the Iraq war was a mistake compared with 52% of all Americans. Eighty-seven per cent of Jews voted for the Democrats in 2006, and all but four of the Jews in Congress are Democrats.

Dissenting voices

An even bigger threat to AIPAC comes from the general climate of opinion. It is suddenly becoming possible for serious people—politicians and policymakers as well as academics—to ask hard questions about America's relationship with Israel. Is America pursuing its own interests in the Middle East, or Israel's? Should America tie itself so closely to the Israeli government's policies or should it forge other alliances?

Zbigniew Brzezinski, a former national security adviser, worries that America is seen in the Middle East as “acting increasingly on behalf of Israel”. Condoleezza Rice, the secretary of state, has compared the situation in Palestine to segregation, and argued that there could “be no greater legacy for America than to help bring into being a Palestinian state”. Philip Zelikow, her former counsellor, argues, in diplomatic language, that the only way to create a viable coalition against terrorists that includes Europeans, moderate Arabs and Israelis, is a “sense that Arab-Israeli issues are being addressed”.

The biggest challenge facing AIPAC is how to deal with this changing climate. Its members have been admirably honest about their mission in life. They boast about passing more than a hundred bits of pro-Israel legislation a year. But they are too willing to close down the debate with explosive charges of anti-Israel bias when people ask whether this is a good thing. America needs an open debate about its role in the Middle East—and AIPAC needs to take a positive role in that debate if it is to remain such a mighty force in American politics.

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Latin America and the United States

A cautious welcome for the gringo

Mar 15th 2007 | CARACAS, MEXICO CITY AND SÃO PAULO
From The Economist print edition

EPA

George Bush's new-found sympathy for social justice in Latin America has prompted a copycat tour from Hugo Chávez

Get article background

IN THE twilight of George Bush's presidency, the word “surge” has come to mean a belated attempt to make up for past mistakes. That applies to Iraq, but also to Mr Bush's week-long, five-country tour of Latin America, which ended on March 14th. His longest trip to the region seemed designed to correct the impression that the United States is too busy battling terrorists to pay much attention to the struggles of Latin American democracies to overcome poverty and drug-fuelled crime.

Mr Bush did not have much new to offer, except in vocabulary: he talked of “social justice”, and of health, education and aid. He visited markets and Mayan ruins, and ate barbecues and guacamole. Predictably, he was greeted with angry (but mainly small) demonstrations. More importantly, he showed that the United States has partners in the region, even among left-leaning governments.

Venezuela's Hugo Chávez did his best to prove the opposite. In a counter-tour which seemingly grew on the hoof to take in a matching, but different, five countries, the populist strongman mocked the American president as a “political corpse” in a Buenos Aires football stadium, denounced the United States as the “most murderous empire in all of history” at a press conference in Port-au-Prince and called capitalism “hell” in a flood-struck town in Bolivia.

In this motorcade joust Mr Bush came out ahead. That is not because the United States is the bigger benefactor but because nowadays its designs in Latin America are less imperial than those of Mr Chávez.

Mr Chávez has one objective: to forge a united anti-American block under his leadership. Mr Bush had several aims. In Brazil, it was ethanol. Aware at last that oil is climate-changing and controlled by unfriendly potentates like Mr Chávez, Mr Bush wants to cut the United States' future petrol consumption by a fifth in ten years. Brazil is already there: 40% of the fuel in Brazilian cars is made from sugar cane.

Mr Bush and Brazil's president, Luiz Inácio Lula da Silva, agreed to promote ethanol production and use across the region, and to co-operate on research. By fixing purity standards, they hope to make ethanol a globally tradable commodity. But Mr Bush refused to talk about the high tariff that protects American corn farmers, whose ethanol is more costly and carbon-emitting to produce than Brazil's.

There was no visible progress on the Doha round of world trade talks, though the American trade

representative, Susan Schwab, spent an extra day in São Paulo to talk to Brazilian officials and industrialists. And Lula, somewhat mystifyingly, insisted that “we're going firmly toward finding the so-called G-spot for making a deal.”

Far from the confrontation desired by Mr Chávez, relations between the biggest powers of North and South America are coming to resemble those between the United States and Europe: there is a recognition on both sides that the overall friendship counts for more than any disagreements on detail. Lula is to visit Mr Bush at Camp David on March 31st.

“This level of presidential diplomacy is unheard of,” points out Paulo Sotero, director of the Brazil Institute at the Woodrow Wilson Center in Washington, DC. “It's very important for Brazilians to be recognised in a special way by the United States vis-à-vis the rest of the continent.”

For Uruguay's leftish president, Tabaré Vázquez, hosting Mr Bush was a tacit message to neighbouring Brazil and Argentina, two of his partners in the Mercosur trade grouping, not to take his small country for granted. Uruguay recently signed a Trade and Investment Framework Agreement with the United States. Mr Vázquez would like that to lead to a free-trade deal, though many in his government, not to mention the United States' Congress, do not.

Mr Bush's seven-hour stopover in Bogotá was the first visit by an American president to Colombia's capital since 1982. That was intended to show that American aid to fight the drugs trade and leftist guerrillas, combined with the tough security policies of President Álvaro Uribe, are making the country safer. Even so, 20,000 troops and police were deployed to secure Bogotá's normally tranquil streets.

In Guatemala, the mood was soured by the arrest in Massachusetts this month of hundreds of illegal workers, many of them Guatemalan. Oscar Berger, the president, told Mr Bush that deportations of illegal migrants should end.

Mr Bush said he hoped an immigration reform bill can be approved in the Senate by August. Until then, the American plan to fence out illegal immigrants will cast a shadow over what ought to be a warm friendship between Mr Bush and Felipe Calderón, Mexico's new conservative president. “The United States has a lot to do to regain respect in Latin America,” Mr Calderón bluntly remarked.

Mr Bush tried. He boasted that he had doubled aid to the region, to $1.6 billion. That is only because of an accounting quirk in 2001. The United States has ramped up aid to a few countries, via Plan Colombia, AIDS programmes and the Millennium Challenge Account (for the poorest). But it has cut development aid to a larger group, notes Joy Olson of the Washington Office on Latin America, a left-leaning NGO. Overall, Mr Bush has spent more than his predecessor, Bill Clinton.

Mr Chávez is outspending and out-promising Mr Bush. He said that Venezuela's cheap-oil deals with its neighbours total 200,000 barrels a day (worth perhaps $1.6 billion a year); in addition, he has announced aid totalling some $5.5 billion. Jamaica, added to his tour (along with Haiti) at the last minute, was promised cheap natural gas. Argentina's president, Néstor Kirchner, thanked Mr Chávez for

helping “at the most critical moments.”

But most of Mr Chávez's neighbours are not enthusiastic about his leadership nor willing to turn their backs on the United States. Lula's coming trip to Camp David is a sign that Brazil will not be bullied into an anti-American axis. Mr Bush wisely ignored Mr Chávez's taunts. No one will miss the United States' lame duck president more than the Venezuelan.

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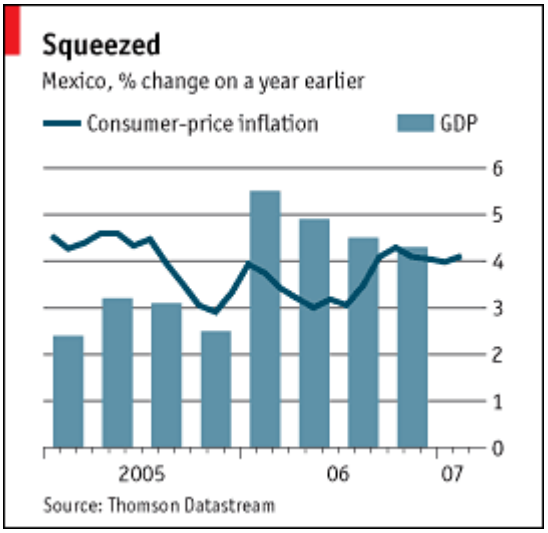
Mexico's economy

Raise or see?

Mar 15th 2007 | MEXICO CITY
From The Economist print edition

A delicate dilemma for the central bank



"ONE thin dime won't even shine your shoes," sang the Drifters. The song might not be well known in Mexico, but the sentiment surely is. After several years of low inflation, prices have been rising more quickly. That is doubly awkward for Felipe Calderón, the new president. Rising inflation is bad news for many of the 45% of Mexicans who are poor. And it comes just as the American economy, to which Mexico's is closely linked, is slowing.

In the 12 months to February, inflation reached 4.1% (see chart). That is far from the triple-digit figures of the 1980s. But it is above the central bank's target of 3%. The main culprit is the higher cost of food staples. In particular, the fashion for ethanol has pushed up world prices for maize and sugar. That is good news for farmers—but not for urban Mexicans.

Having risen sharply before Christmas, the price of maize tortillas fell by 10% in the second half of January. Gray Newman of Morgan Stanley, an investment bank, argues that the spike in food prices will not translate into a longer-term rise in inflation.

The central bank must surely hope so. It has not altered its monetary-policy stance: benchmark interest rates fell last April and have been unchanged since. With economic growth already slowing, the bank's governors will be hesitant to raise rates at their next meeting on March 23rd, says Damian Fraser of UBS, another investment bank. Others are not so sure.

Guillermo Ortiz, the bank's long-serving president, has the confidence of markets. Agustín Carstens, the new finance minister, comes from the IMF and is widely respected. Mexico's economic credibility has been hard-earned. It is now being put to the test.

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Ecuador

Correa v Congress

Mar 15th 2007 | QUITO
From The Economist print edition

A conflict of powers hits the streets

Get article background

HE HAS been in office for only two months, but already Rafael Correa, Ecuador's president, has provoked a full-blown conflict of powers that pits the country's Congress against its courts. The immediate issue is his plan for a Constituent Assembly, whose job would be yet another rewriting of the constitution, which dates only from 1998. The real battle is for power, between Ecuador's political parties and Mr Correa, who calls himself a Christian leftist and is a friend of Venezuela's Hugo Chávez.

On March 7th, the electoral tribunal decided, by three votes to two, to expel 57 opposition legislators from Congress. The previous day they had backed moves to sack the head of the tribunal because he had used his casting vote to call a referendum on the new assembly. That was a job for the legislature, they said. Both decisions were of dubious legality.

The action moved to the streets. The police stopped the 57 from entering Congress. When they tried to meet at a hotel, Mr Correa's supporters beat up one and attacked another's car. The next day, two legislators were injured in a clash with police. The Constitutional Court, the highest legal body, has declined to rule on the dispute. Mr Correa wants to replace the sacked legislators with their designated alternates.

Both Congress and the president were chosen in the same general election last year. The president's main weapon is his popularity: polls give him an approval rating of over 70%. He promises a “citizens' revolution” against a corrupt “partyocracy”. His own improvised party did not take part in the congressional election.

Mindful of Mr Correa's popularity, Congress did not block the referendum. But it did try to include a provision which would stop any assembly from booting out elected authorities. But that, of course, is precisely what Mr Correa wants it to do.

The president will probably get his way. But not necessarily for long. He is picking fights on all sides: with newspaper editors, businessmen and the political leaders of Guayaquil, the economic capital. Ecuador is a fractured country, with many regional power bases. That has meant that Congress, not the presidency, has often been the locus of power. Legislators have ousted two presidents since 1997. Lucio Gutiérrez, toppled in 2005, is emerging as Mr Correa's most powerful opponent. The president is winning a battle, but not yet the war.

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About sponsorship

Wine in Argentina and Chile

Vino's twin peaks

Mar 15th 2007 | MENDOZA AND SANTIAGO
From The Economist print edition

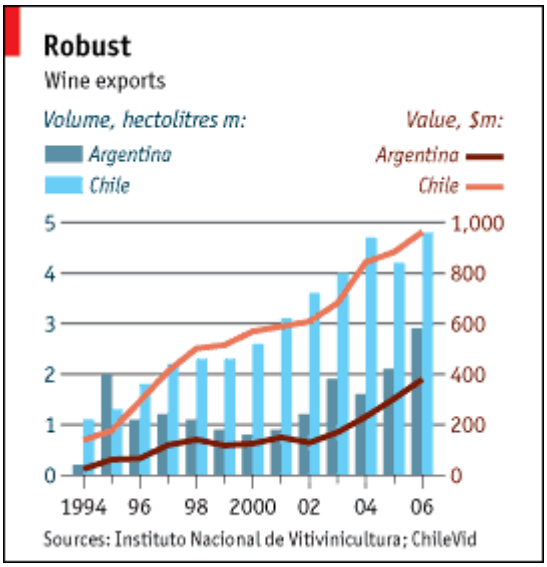
Argentina is catching up with Chile—but not as fast as it might

EARLIER this month, 70,000 visitors descended on Mendoza, Argentina's wine capital, for the annual festival marking the start of the grape harvest. Locals crammed the hilltops surrounding the city's packed amphitheatre, to watch the dancing and the beauty pageant. They had much to celebrate: in the past four years, Argentina's wine exports have more than doubled in volume and have tripled in value.

Until fairly recently, Argentina was a backwater for oenophiles. It was a big producer of low-quality table wines for local quaffing. That is changing fast, especially since a devaluation in 2002. Foreign investment has poured in and exports have boomed. Thanks partly to the arrival of foreign winemakers, quality has greatly improved. Nowadays Argentines themselves drink beer and less, but finer, wine.

Yet a glance across the Andes, whose towering, snowcapped peaks form the dramatic backdrop to Mendoza's festivities, ought to temper the euphoria. Neighbouring Chile became an important wine exporter a dozen years before Argentina. And it still has a big lead (see chart).

One might think that Argentina ought to be winning this battle hands down. It is the world's fifth-biggest wine producer, and has endless suitable land. Chilean winemakers envy their neighbours' trademark Malbec grape, which produces a potent red wine that has become known across the world. Fresh, perfumed whites made with Torrontés grapes, mainly around Salta, are similarly distinctive, if less complex. By contrast, Chile exports mostly standard varieties, such as Cabernet Sauvignon and Chardonnay, which are widely produced across the world. Its only unique grape is Carmenère, from which it is far trickier to make good wine.



Argentina's exports to the United States are growing much faster than those of Chile. That may be partly because its robust, fruit-packed wines are to American taste. *Wine Spectator*, the bible for American oenophiles, gives ratings of 90 points or over (out of 100) to 172 reds from Argentina, compared with 138 from Chile. The $120-a-bottle top wine of Achával-Ferrer, a locally-owned boutique vineyard, was recently given a 95.

But Chile has some powerful strengths of its own. A wealth of different *terroirs* nestle among secluded valleys; cool Pacific breezes make it possible to produce fine white wines as well as reds. And last year *Wine Spectator* gave 96 points to Don Melchor 2003, the top Cabernet from Concha y Toro, the largest wine firm.

Chile's greater economic stability has also helped. “With quality wines, you need 15 to 20 years for an investment to mature,” says Aníbal Ariztía of the main winegrowers' association. Since 1995, the area under vines in Chile has doubled to 100,000 hectares (250,000 acres). In Argentina, the total area has remained static, though vine quality has improved.

Perhaps Chile's most important advantage is its export vocation. Its web of free-trade agreements has helped, not least because of the (sometimes negative) media coverage these have generated in importing countries. Chile's wine exports to South Korea took off when farmers there demonstrated

against a trade agreement. Wines of Chile, a trade body, opened an office near London in 2002. Since then Chile's market-share in Britain (the world's biggest wine importer) has risen from 5% to 7%, says Ricardo Letelier, its general manager. It plans an office in the United States and hopes to boost worldwide exports to $1.2 billion by 2010, with most of the growth coming from higher prices.

Yet paradoxically, marketing is where Argentina has an unexploited edge. Chile has built a reputation for reliable, good-value wines. But its marketing men worry that its ability to command higher prices is restricted by the lack of a clearer country image. “Argentina has the tango, Evita and Maradona; Chile doesn't have their equivalent,” agrees Patricio Tapia of *Wine & Spirits*, a New York-based magazine. While Argentina's winemakers have yet to unite in a single trade body, the industry did open a London outpost last year.

Both countries' wine exports—especially Argentina's—have the potential to carry on growing. But not all producers will thrive. Chile's are battling with a strong currency (the result of high copper prices). Mr Letelier reckons that most of the country's 150 exporters are barely managing to cover costs at the moment. Their smaller local market offers less of a cushion, though some have sought to diversify by investing in Argentina.

Argentine winemakers may face bigger headaches. Record profits have attracted a flood of new investment. But double-digit inflation has caused wages and the cost of inputs to soar. José Manuel Ortega, of O. Fournier, a Spanish vineyard in Mendoza, reckons that the cost of building a winery has quadrupled in dollar terms since 2002. A 5% tax on wine exports and the government's lack of interest in trade agreements are further obstacles. That points to a coming shake-out: Mendoza alone has more than 800 separate producers. But for now, variety and innovation continue to thrive on both sides of the Andes.

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Security in Asia

We're just good friends, honest

Mar 15th 2007 | BEIJING AND TOKYO
From The Economist print edition

Claudio Munoz

But China has reason to suspect Japan's military flirtation with Australia

Get article background

WHEN he signed a security pact with Australia this week, Shinzo Abe, the Japanese prime minister, at a stroke doubled the number of Japan's allies. Until now, Japan has had formal security ties only with America, under whose protection Japan, with a pacifist constitution, has sat since the second world war.

Even if it falls well short of a mutual-defence treaty, to some Australians the agreement signed by John Howard in Tokyo on March 13th is unwarranted. After all, Japan came close to invading their country during the war; Australian prisoners-of-war were brutally treated in Japanese camps; and only a couple of weeks ago Mr Abe had brought ignominy upon himself by denying that foreign “comfort women” had been coerced into working in wartime military brothels. Elderly Australian women are among those who have testified otherwise. Yet the world moves on and in Mr Howard's view “Australia has no better friend or more reliable partner within the Asia-Pacific region than Japan.” Mr Abe spoke of a “shared destiny”.

So if it is now important that the two countries be allies, the natural question is, against whom? To ask this, both sides insist with prim faces, is entirely to miss the point. Co-operation between the two countries has deepened on several levels. Until last July, Australian troops had protected Japanese ones doing reconstruction work in southern Iraq. Nearer to home, peacekeeping troops have worked side-by-side in Cambodia and Timor-Leste.

Alexander Downer, the Australian foreign minister whose own father was a prisoner of the Japanese for more than three years, talks up their co-operation in disaster assistance after the Indian Ocean tsunami of late 2004. The two countries' aid programmes in Asia have shared objectives. Thus the agreement's provisions for regular meetings involving the two sides' foreign and defence ministers, joint military exercises, and more formal arrangements for sharing information would all improve humanitarian missions.

A security agreement is a symbolic way of building up those new aspects of the relationship, says Mr Downer. The two sides will also negotiate a free-trade agreement to strengthen economic ties. All good stuff. But the louder the denials from both sides, the more evident is the main catalyst for the security

pact: the rise of China.

That may come as a surprise to some. Australia has often had to defend itself against charges from human-rights groups and others of sacrificing democratic principles for profits in its dealings with China, which has an inexhaustible appetite for the commodities, such as iron ore and uranium, that Australia is able to supply. But as an Australian diplomat explains: “China is a good, constructive commercial partner, but in terms of ideas and values, it will never be anywhere near as close to us as Japan. It's quite clear: Japan is our best friend in Asia.”

Australia's security posture has long been a cause for wariness in China, particularly because of its alliance with America and the possibility that Australia might come to America's aid in a war with China over Taiwan. Still, as long as the new pact does not imply Australian support for Japan in its territorial disputes with China in the East China Sea, China's government will attempt to hide its displeasure. Economic ties come first.

As for Mr Abe, the pact is of a piece with a more robust foreign policy for Japan that was begun by his predecessor, Junichiro Koizumi. Before sending troops to Iraq, Mr Koizumi had also dispatched supply ships from Japan's so-called Self-Defence Forces to the Indian Ocean to help with the war in Afghanistan in 2001.

Since he came to office last September, Mr Abe has redoubled Mr Koizumi's commitment to Japan's alliance with the United States, but wants to do more than just shelter under America's wing. He has pushed for faster deployment of missile-defence systems in the face of North Korean provocation. He has turned the Japanese Defence Agency into a full ministry, with a seat in the cabinet. And he wants the pacifist article nine of the constitution to be revised. Mr Abe has sought a new partnership with India, while building security ties with South-East Asia.

It all amounts to a strategy of balancing China's geopolitical reach: Japan, in other words, is not about to roll on its back to let China be the region's top dog. Mr Abe's domestic ineptitude may mean a short term in office, as the ruling Liberal Democratic Party and its coalition partner face crucial elections for parliament's upper house in July. Even if so, Japan's emerging regional posture is likely to survive him.

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Democracy in China

Hong Kong's make-believe election

Mar 15th 2007 | HONG KONG
From The Economist print edition

Nobody doubts that Donald Tsang will be returned as chief executive. But China is under pressure to allow a more open contest next time

Get article background

THE people of Hong Kong were treated to a startling sight earlier this month: their Beijing-approved leader, who is up for re-election, was arguing it out live on television with a pro-democracy challenger seeking his job. Despite the appearance of a genuine contest, however, real democracy has not yet arrived.

EPA

Let's pretend this is an election

The selection of a chief executive for Hong Kong is still a choreographed affair that will return China's man, Donald Tsang, with a big majority. The candidates may be pressing the flesh in housing estates, but the public has no direct say in the matter. Instead, the choice will be made on March 25th by a committee of 800 members, mainly pro-Beijing politicians and worthies chosen by business and professional groups that shun confrontation with the authorities in China.

Yet things are changing. To democrats' surprise, a new election committee chosen last December had just enough members of the right bent to enable a pro-democracy candidate—Alan Leong, a barrister and a member of the local mini-parliament known as the Legislative Council (LegCo)—to be nominated for the first time.

In the last two elections for chief executive there was no contest and, according to Mr Leong, the government in Beijing had not expected opposition this time either. Mr Tsang is now having to put on a show of electioneering. In the televised debate on March 1st with Mr Leong, he appeared uncomfortable and defensive. Mr Leong noted that the public had not been invited to the event; only members of the election committee were allowed in and the few pro-democracy protesters who burst into the venue were bundled out. Another debate was due to take place on March 15th with questions from the public. Mr Leong says the political landscape of Hong Kong has been changed for good; no chief executive could expect to be elected again without having to face the people.

The election comes at a crucial juncture in Hong Kong's post-colonial development. According to the Basic Law, Hong Kong's mini-constitution which was approved by China in 1990 and took effect when the British left in 1997, the territory's ultimate aim is to have universal suffrage. Many in Hong Kong had thought this could happen this year for the chief-executive election, and next year for the semi-democratic legislature.

But China's rulers decreed three years ago that Hong Kong would not be ready for democracy so soon. Pressure is now growing on Mr Tsang to set a target date. In the televised debate (seen in parts of the mainland), Mr Tsang avoided giving any such timetable. He says his government will issue a green paper later this year setting out ways of expanding democracy. Then, after three months of public discussion (he says he hopes to complete this by Christmas), the government will produce a single preferred option to submit to the authorities in Beijing. Mr Tsang says he will bow to the public will, but he says opinion polls show that 65% of Hong Kong people think they would not be ready for full democracy when chief-executive and legislative-council elections are held in 2012.

Mr Leong's Civic Party, which was formed last year, and other pro-democracy groups demand universal suffrage by then. Some democrats fear the government will use the public consultation in the same way the British-era government used a similar exercise in the late 1980s to delay reform. Anson Chan, who retired six years ago as chief of Hong Kong's civil service and enjoys huge popularity, has proposed a more gradual move to full democracy in 2016, but even her ideas have been received coolly in Beijing. She argues that Hong Kong is inherently unstable: at present there may be a feel-good factor thanks to the economic upturn of recent years, but the next slump could bring a groundswell of discontent unless there is quicker progress to democracy.

A big obstacle to any reform is LegCo, two-thirds of whose members have to support any political change. In 2005, pro-democracy members managed to block a package of limited government-inspired reforms, saying they wanted far more. But pro-business members, who tend to support China's stance, could block any attempt to change the current make-up, which reserves half the seats for business and professional groups. A major worry for them is that a fully democratic LegCo might demand more welfare spending and raise the cost of doing business.

Mr Tsang says Hong Kong is nowhere near finding consensus on reforming the legislature. But he says there are the makings of a deal over his job: instead of choosing the chief executive, the election committee could draw up a list of candidates to be voted on by the public.

Allowing the public its say may not give power to the democrats. Mr Tsang lacks charisma, but opinion polls suggest he would win a comfortable majority because of his experience—and his ability to get on with those overseers in Beijing.

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Taiwan

Cultural revolution

Mar 15th 2007 | TAIPEI
From The Economist print edition

The fight over a dictator's legacy

Get article background

CHIANG KAI-SHEK may once have been revered as a near-god on Taiwan, where he led his Chinese Nationalist regime after being defeated by Mao Zedong's Communists on the mainland in 1949. But almost a third of a century after his death, the memory of the old dictator is being effaced, with the removal of the generalissimo's statues and the renaming of many streets and even Taipei's international airport.

This has provoked a political row, which this week engulfed Taiwan's defence minister, Lee Jye. He was expelled from the Kuomintang (KMT), Chiang's former ruling party, for allowing statues of the old nationalist to be removed from Taiwan's military bases.

Reuters

No longer mourned

Chiang's legacy has never been properly examined in Taiwan. Arguments about the past are also fights over what the island should be in the future: a part of China (the view of Chiang Kai-shek and his political heirs), or an independent nation with a distinct, non-Chinese Taiwanese identity.

The current government of President Chen Shui-bian, whose Democratic Progressive Party (DPP) leans towards independence (but which appointed a KMT man as defence minister), intensified its campaign against the generalissimo as the island marked the 60th anniversary of the “228 Incident”—the KMT's violent suppression of protests against its rule on February 28th 1947. An estimated 28,000 were killed.

Blaming the massacres on Chiang and the “outside” regime of the KMT, the DPP announced plans to rename the giant Chiang Kai-shek Memorial Hall in Taipei as the “Taiwan Democracy Memorial Hall”, and tear down the sanctuary's perimeter wall. The central government dropped “China” from the names of many state enterprises last month. There is talk of removing Chiang's portrait from Taiwanese coins.

DPP leaders may be politicking ahead of parliamentary elections in December, and presidential polls next March. But there is more at stake. By casting the 228 Incident as a clash between Taiwanese and KMT “outsiders”, the DPP has not only opened old wounds in Taiwan but also created anxiety in Beijing. China's Communists may have been at odds with the generalissimo. But they fear that Taiwan, by breaking with Chiang's legacy, may also be breaking away from the Chinese mainland.

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Fiji and Tonga

A tale of two island states

Mar 15th 2007 | SUVA
From The Economist print edition

And of their contrasting attitudes to democratic reform

Get article background

THE Pacific archipelagos of Fiji and Tonga have for centuries been connected by trade and kinship: Tongan princes sailed westwards in outrigger canoes to seek fortune in Fiji, while Fijians provided spouses for the Tongan nobility. These days, the two island states are in the throes of domestic crises, but they are tackling them in strikingly different ways.

In Fiji, the new prime minister, Commodore Frank Bainimarama, the military commander who seized power in a coup in December, is resisting international pressure to return to democracy speedily. He says he needs time to clean up the corruption left by the previous, elected, government. By contrast in neighbouring Tonga, last November's riots in the capital, Nuku'alofa, have not been allowed to derail plans for democratisation.

Commodore Bainimarama has sacked all the previous parliamentarians and has purged top civil servants. Dismissals and suspensions have often taken place on the flimsiest of evidence. Soldiers, installed in a new complaints centre, listen to public grievances and send out vigilante missions to tackle everything from village quarrels to landlord-tenant difficulties and domestic disputes.

Scores of alleged bootleggers, drug pushers and prostitutes have been rounded up, while opponents of the new order have been beaten up at the army's Queen Elizabeth Barracks in Suva. Yet the emphasis on rounding up the small fry looks increasingly like a deliberate distraction from the army's failure to prove its coup-justifying claim of widespread corruption in the ousted government.

Tonga is moving in the opposite direction. After a century of royal rule, in which the monarchy defended its power with claims that government by the masses would prove “corrupt”, political leaders are coming around to the view that more democracy is the best way to check mismanagement and improve Tongans' living standards.

Until recently, the cabinet was composed entirely of the king's nominees, and only nine popularly elected representatives sat in the 30-member legislative assembly, alongside nine noble representatives and 12 members appointed by the king. The royal government squandered money on misguided aviation and shipping ventures, and the bulk of the $56m it secured from selling passports was frittered away in poor investments by a visiting American rogue rather quaintly appointed by the king as his “court jester”. That the royal family also benefited from big private-sector investments—including ownership of the mobile-

phone industry, cable television, a brewery and the electricity utility—increased public disquiet.

The monarchy responded with a pragmatic reform programme that began before the accession of King George Tupou V to the throne in September 2006. Elected members of parliament were allowed to enter the cabinet, and for the first time in a century a “commoner”, Fred Sevele, became prime minister.

Still, reformists are impatient and have taken to the streets. A rally outside parliament in November exploded into riots that devastated Nuku'alofa. Some 80% of the capital's business district was destroyed and six rioters died. Yet the king promised to press ahead with reforms.

Although both Fiji and Tonga have experienced severe instability in recent months, the latter seems to have a better idea of how to weather it. In the view of Peter Larmour, a specialist on the Pacific islands at the Australian National University in Canberra, corruption is better tackled by reducing institutional opportunities for it, rather than by dictatorial moral crusades from a strong-arm regime that sets itself up as detective, judge and juror.

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The Philippines

Latin upbeat

Mar 15th 2007 | ZAMBOANGA AND BASILAN
From The Economist print edition

A peace dividend in Mindanao

“WELCOME to Asia's Latin City”, proclaims a giant poster at Zamboanga's airport, beside a smiling picture of the mayor, Celso Lobregat. This does not refer to the port city's reputation for Colombian-style lawlessness, but to its Spanish-derived dialect.

Locals claim Zamboanga has been unfairly tarred by its proximity to the Sulu archipelago, stronghold of Abu Sayyaf, the al-Qaeda-linked separatist group with a nasty sideline in abductions and banditry. Business has not been helped by the fact that foreign tourists and Christian missionaries have been among the victims of violence. These days, though, Zamboanga is enjoying a modest peace dividend, thanks to an American-supported military campaign against Abu Sayyaf.

This operation began on the island of Basilan in 2002, and has since moved to Jolo, where Philippine troops claim to have killed or captured as many as 200 militants since August. The 450 or so American soldiers keep a low profile. They were nowhere to be seen last month when a European cruise ship carrying elderly German tourists docked in Zamboanga, the first such vessel to visit since 1998.

In 2005, the Zamboanga peninsula was the fastest growing region in the Philippines, with GDP growth of 7.2%. There are no more recent data, but Mr Lobregat points to more good news such as two new outlets of Jollibee, a Philippine fast-food chain. Teresita Sebastian, regional manager of the Philippine National Bank, says bank deposits are climbing, though loan growth is still modest. Three new shopping malls are going up in the city centre.

Such prosperity is less apparent on Basilan, a 30-minute ferry ride away. Local businessmen fret about crime, despite a fall in kidnappings and bombings since the expulsion of Abu Sayyaf in 2002. Tensions are rising ahead of local elections in May. Politicians are accused of beefing up their private armies, a standard and troubling feature of Philippine elections. Last year the mayor of Isabela, the island's capital, was shot dead outside his office by an allegedly deranged Muslim gunman. Two prominent political clans, one Muslim, the other Christian, are vying to replace him. Plainly, the region's troubles run deeper than just those in Abu Sayyaf.

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Pakistan

Poor judgment

Mar 15th 2007 | ISLAMABAD
From The Economist print edition

How General Musharraf upset the lawyers

Get article background

THE enemies of General Pervez Musharraf, Pakistan's president, are multiplying. Militants want to kill him, political parties seek to drive him from power and, in recent weeks, his American allies have expressed doubts about his counter-terrorism efforts. This week, the attack came from a new quarter: Pakistan's lawyers, who began unruly protests across the country to denounce the president's attempt to sack the country's top judge, Iftikhar Chaudhry, on March 9th.

Summoned to Army House, General Musharraf's den in Rawalpindi, Mr Chaudhury was strongly advised to resign. When he refused, he was suspended by a hastily convened gang of five fellow supreme-court judges. He was then confined to his home. The charges against Mr Chaudhry, which were heard by judges behind closed doors on March 13th, are believed to include abuse of office and other kinds of misconduct.

AP

Defending the law

A wave of sympathy for the judge, and antipathy towards the general, is sweeping the country. In Islamabad, Lahore, Karachi and elsewhere, besuited lawyers boycotted the courts and clashed with baton-waving police outside them. Diplomats say privately that if Pakistan's exiled civilian leaders, Benazir Bhutto and Nawaz Sharif, can bring out their supporters to join them on the streets, the protests might pose a real threat to the general's position.

The army's effort to subjugate Pakistan's northern tribal areas is one reason for the general's fading popularity; it made him look like an American puppet, and seems to have provoked a wave of terrorism, including six recent suicide bombings, in Pakistan's main cities. Another is the latest attempt by the president to twist the country's judiciary to retain power. General Musharraf has declared his intent to get re-elected as president by the current parliament and not, as the opposition reads the constitution, by the next legislature, following elections due in November. Another dispute revolves around his refusal to give up his military uniform.

In the two years since General Musharraf appointed him, Mr Chaudhry has done more or less everything a Pakistani judge is not supposed to do. He has launched inquiries into the disappearance of suspected insurgents in Balochistan; he has castigated ruling politicians and police chiefs for abandoning the poor. He banned ostentatious wedding ceremonies because they provoked class hatred. He heard petitions against inflation, stopped public parks from being converted into golf clubs for the rich and outlawed child marriage. Last year he especially annoyed the president by stopping the privatisation of a big steel company, because of irregularities in the bidding process.

If General Musharraf indeed intends to remain army chief and president for another five years, he can expect a flood of legal challenges. In anticipation of this, an independent-minded top judge was clearly not to his taste. But the result of Mr Chaudhry's suspension creates an even bigger mess in Pakistan. If Mr Chaudhry is sacked, General Musharraf will find it even more difficult to claim that his rule is constitutional; if Mr Chaudhry is restored, he might become an even bigger headache for the general. With such troubles ahead, many Pakistanis wonder whether the scheduled elections will even be held.

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Zimbabwe

The face of oppression

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AFP

Another ugly political crackdown. But also signs of hope

THE opposition in Zimbabwe suffered another grievous blow this week. On March 11th, Morgan Tsvangirai, the leader of the main opposition party, the Movement for Democratic Change (MDC), was arrested together with about 50 protesters and opposition leaders. He was on his way to a prayer rally organised by the Save Zimbabwe Campaign, a group of political, religious and civic groups pushing for political change. But security forces were waiting and grabbed Mr Tsvangirai before the rally even started, sparking clashes with hundreds of assembled protesters.

One activist was shot dead and Mr Tsvangirai, who limped into court with a swollen face and a nasty head wound two days later, was badly beaten up while in police custody, as were others detained with him. Following his short court appearance, when he was greeted by cheers from his supporters, he and several others were taken to hospital to have their wounds looked after. Mr Tsvangirai himself was admitted to the intensive-care unit with a possible skull fracture, but vowed to continue the struggle against President Robert Mugabe. Their ill-treatment provoked outrage from the UN, the European Union and America—but not, as usual, from Zimbabwe's immediate neighbours, such as South Africa.

Mr Tsvangirai's arrest is the latest episode in a series of failed protests. Sporadic street marches organised by trade unions, NGOs and other pressure-groups have been violently dispersed over the past few months, and their leaders have been routinely arrested and beaten up. Mr Mugabe's government recently banned all political rallies and the regime has become increasingly more repressive and brutal. Nonetheless, trade unions are planning another national strike next month.

They will be following in the footsteps of doctors and nurses who, unable to feed their families, went on strike in January to protest against the plummeting value of their salaries. Inflation, now running at over 1,700%, is the highest in the world and is expected to worsen. Once the regional bread-basket, Zimbabwe is again going to go hungry this year. The economy has shrunk by half since 1999, and unemployment is thought to be at least 80%. Many people survive thanks to the black market and money or food sent by the 3m or so Zimbabweans who have left the country.

Despite the attempts to protest on March 11th, the disparate opposition has so far been too weak to organise mass rallies or demonstrations. The MDC even split in 2005, although recently it has been trying to mend its divisions. Change is more likely to come from within the ranks of the ruling ZANU-PF, which itself is showing signs of cracks. At the party's annual congress last December, Mr Mugabe suggested that presidential elections, expected next year, should be organised instead alongside parliamentary ones

in 2010. But several delegates reacted with something less than the usual enthusiasm to this idea; it was put on hold until a meeting of the party's central committee which is due to be held later this month.

During an interview for his 83rd birthday bash last month—for which the government spared no expense—Mr Mugabe openly acknowledged the growing tensions within ZANU-PF by lashing out at the various factions within the party, accusing them of vying for power. Particular targets of his wrath were his vice-president, Joyce Mujuru, and her husband, an influential ZANU-PF stalwart who used to head the army.

Divide and rule

Mr Mugabe had kinder words for Emmerson Mnangagwa, once the speaker of parliament, who is also thought to be a presidential hopeful. The International Crisis Group, a pressure-group based in Brussels, argues that there is now a chance that Mr Mugabe will be forced into retirement by his own party, leading to a power-sharing government between moderate ZANU-PF leaders and the MDC until elections can be organised under a new constitution.

It may not be as simple as that, however. Mr Mugabe has now said that, if elections were to take place next year, he would be ready to run again, despite earlier suggestions that he would retire. It is by no means certain that rivals within his own party—moderate parts of which are said to be talking to the MDC—can muster enough muscle to push him to go. Mr Mugabe still commands deep-seated loyalty within the army and the intelligence services. Although the security forces are also suffering from the country's economic disintegration, key units such as the presidential guard receive special treatment.

Those within ZANU-PF keen to see Mr Mugabe retire have also been divided among themselves. Mr Mnangagwa tried to block Mrs Mujuru's appointment as vice-president in 2004. The former speaker is making a political comeback, but this may be little more than a shrewd attempt by Mr Mugabe to weaken the Mujuru faction, whose ascendancy he now resents.

What is certain is that Mr Mugabe has so far shown no appetite whatsoever for leaving office. The idea to postpone the presidential election until 2010 could well be dropped, as it will be hard to obtain enough votes in parliament to secure the necessary constitutional amendment. But the alternative is likely to be a presidential election next year. If Mr Mugabe runs in that, and the election is as rigged as previous ones, Zimbabweans may have worse to look forward to.

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Uganda

America's friend

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But sending troops to Somalia cannot paper over the cracks at home

AFP

Ugandan troops to the rescue

ON THE whole, life in Uganda has been improving. In the past year, the Lord's Resistance Army, a sadistic rebel militia which had made a hell out of the north of the country for two decades, retreated to Congo and has been drawn into peace negotiations, albeit fitfully, with the government. For the first time in a decade, 1m or so northerners may be able to leave the dismal camps where they had been forced to take shelter. The rains have been plentiful, alleviating a drought. And, perhaps best of all, the country came through an election unscathed, though President Yoweri Museveni arm-twisted his parliament into changing the constitution to let him have a third term in office.

Indeed, Mr Museveni bent just about every rule to stay in power. He meddled with the courts, muzzled the press and brought out his own presidential guard to stymie protests. There were fears that Uganda might slip back into the bloody ways of its past. But it has not happened. Despite a big ego, Mr Museveni is no megalomaniac. Nor has he resorted to the spying tactics and wholesale imprisonment of dissidents that his counterpart to the north-east, in Ethiopia, has done.

Instead, he has cannily sought to boost his reputation with America and the West by contributing 1,600 troops to the African Union peacekeeping force in Somalia. They were the first to land in the capital, Mogadishu, two weeks ago to support the Ethiopian-backed transitional federal government that recaptured the south of the country from Islamist militias last year. The Ugandan troops are now the targets of an Islamist insurgency there.

Mr Museveni has also made himself useful to America by standing up to Sudan over the conflict in Darfur. Some Pentagon observers think Mr Museveni's opportunistic alliance with Ethiopia—whose troops the Ugandans are supposed to replace in Somalia—has the makings of a bulwark against Islamist expansion in the Horn of Africa.

But in return for the diplomatic and military help, Mr Museveni will expect all the Western aid and goodwill that he can get, for his legacy at home has begun to look threadbare. Yes, the government has improved primary education and health care and it has made headway against AIDS. But Uganda's young people, in particular, are at a loss. Half of the 28m-strong population is under 15, and on some projections it could reach 100m by 2050. Mr Museveni thinks this is good. With proper investment it might be, but too much of Uganda is disintegrating or chaotic.

An upturn in Uganda's economic fortunes serves only to highlight how far the country has yet to go. Its economy is set to grow by more than 5% next year, but that is short of the 7-8% needed to reduce poverty noticeably. Many parts of the country have no electricity and even in Kampala, the capital, it is rationed. Mr Museveni says he will not tolerate “even a single day's delay” in bringing new power stations on stream. Don't bank on it.

The greed of Uganda's well-equipped armed forces has made a big hole in the national budget. And Mr Museveni's habit of giving plum jobs to chums and relatives is costly too. But the main problem, these days, is a failure of vision. Neither the government nor foreign donors seem to know how to bring about the massive infrastructure improvements the country needs if it is to progress. The government shows no urgency in building new transport links with Kenya or Congo. Nor does it make the most out the resources it does have, such as Lake Victoria. As elsewhere in Africa, Mr Museveni has done well at playing off sweet but dithering Western donors against sour but relentless Chinese entrepreneurs. Yet farming, forestry and new-found oil have the potential to fuel faster economic growth.

Instead, Mr Museveni's focus now is dynastic; he wants to preside over some kind of East African federation, comprising Uganda, Kenya and Tanzania, perhaps with a family member succeeding him in Kampala's State House. With little threat now to his authority from a divided opposition, he is relaxing his grip. Radio talk-shows are vibrant and sometimes critical of government. That should help to burnish his image as a regional statesman at this year's Commonwealth summit in Kampala, as will his troops in Somalia.

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Nigeria

Blood and oil

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Elections could further destabilise the violent, oil-rich Delta region

THE seedy drinking-holes frequented by burly foreign oilmen in Nigeria's main oil city of Port Harcourt are pretty empty these days. Kidnappings and killings of expatriate workers, car-bombs and violent robberies have persuaded many to stay behind the high walls and barbed wire of their own homes, as armed groups wreak havoc ahead of national elections next month.

In the past year, attacks on oil facilities have forced Nigeria to shut down a fifth of its production; over 100 foreign workers have been kidnapped in the oil-producing Niger Delta region. Higher security costs and a shrinking number of expatriates willing to take the risks of working there have sharply slowed new investment. The Nigerian government has lost billions of dollars in oil revenues. Now the multinational oil companies, such as Royal Dutch Shell, that operate in Africa's biggest oil producer are bracing themselves for more trouble. The omens are not good; in the run-up to the elections in 2003, violence in the Delta forced Nigeria to shut down 40% of its oil capacity.

Trouble in the region is not a new phenomenon, but it has escalated in the past year or so. For years, impoverished communities in the tropical swamplands of the Delta protested against exploitation of their lands by oil companies, only to be suppressed by the army. Things got worse under civilian rule in the late 1990s, when politicians armed local thugs to rig elections for them. After the 2003 elections, many of these bully-boys used their guns in territorial squabbles in the mangrove creeks. But they also began to espouse a radical political rhetoric as well, demanding a greater share of the oil-wealth for their local communities. In the cities, criminal gangs, born from secretive university fraternities, were armed in a similar way.

Militant cells and gang leaders are engaged in a variety of criminal enterprises, building up arsenals of weapons with the proceeds and sometimes working with corrupt army officials. The theft of crude oil from sophisticated oil pipelines and wells (known as “bunkering”) has become a multi-million-dollar industry. Worryingly, the Movement for the Emancipation of the Niger Delta (MEND), the mysterious group responsible for the most troubling attacks on the oil industry last year, has been trying to bridge the gap between militants in the creeks, with their machine-guns and rocket-launchers, and the criminal gangs in the cities, armed with lighter Kalashnikov rifles.

On January 28th MEND stormed a police complex in Port Harcourt, freeing 125 criminals, including Soboma George, an influential gang leader who had once been used to help rig state elections for the ruling party. MEND's anonymous leader and spokesman boasts that he has “the oil industry by the balls”. On March 15th, after releasing its latest two hostages, presumably for a nice ransom, MEND promised to step up its attacks.

But many groups falling under the broad banner of MEND have local agendas and a variety of paymasters. Some have been enraged by the choice of gubernatorial candidates put up by the ruling People's Democratic Party (PDP) which may well cheat, rig and bribe its way into hanging onto power in the Delta State Houses in April's elections. The richest oil-producing states have revenues of up to $1.3 billion a year but dismal records in providing basic services, since officials loot most of the money. The fear is that militants could work alone or with MEND to disrupt elections in the Delta states and launch attacks on the oil industry as a way of holding the PDP state and federal governments to ransom. “Either bodies are going to pile up or we are going to see an oil shock, or both,” says an oil-industry security official.

The PDP candidate for president, Umaru Yar'Adua, a northern state governor, says that by picking as his running-mate Goodluck Jonathan, from the Delta's majority tribe, the Ijaw, he will be able to tackle the

region's problems. Should he become vice-president, Mr Jonathan will be under pressure to deliver quick results to his people if he wants to stave off yet more violence and unrest in his land.

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Democracy in the Middle East

Regression analysis

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The small gains for democracy are now being rolled back

TWO years ago, President Hosni Mubarak of Egypt declared that he would allow rivals to run against him in the most populous Arab country's first open presidential election. This was hailed as another sign that political sands were shifting across the Middle East, with power in the world's least democratic region at last beginning to pass from long-ensconced rulers to their restive subjects. Some even talked of a democratic revolution.

Other signals included the holding of elections in Iraq and Palestine, the “Cedar Revolution” that shook Lebanon from Syrian control, fairer-than-usual presidential polls in Tunisia, Algeria and Yemen and a widening of the political franchise in several Gulf monarchies. Voices of dissent grew louder, often via new media such as satellite television, even as the Bush administration trumpeted democratisation as the surest foil for extremism.

The sands are still moving, but lately look more like the contents of an hourglass that the same old rulers have turned upside-down. Except for a few brighter spots, the general trend from Morocco to the Persian Gulf has been towards a reinforcement of central control, a curtailing of public freedoms, and a fading of hopes for peaceful democratic change. Egypt itself, a country that is often seen as an Arab bell-wether, provides a useful example.

The runner-up to Mr Mubarak in the 2005 presidential election, Ayman Nour, languishes in prison, charged with forgery. The Muslim Brotherhood, which proved its potency as Egypt's main opposition by capturing a fifth of parliamentary seats that year, remains officially unrecognised. Government harassment of the group, which claims to want an Islamic form of democracy, has intensified, with hundreds of members arrested and dozens awaiting trial before military tribunals.

Mr Mubarak's government is meanwhile pushing ahead with plans to “modernise” Egypt's 1971 constitution. It is true that the changes would abolish outdated verbiage describing Egypt as a socialist state. But they would also formally ban all parties based on religion, so, in theory, shutting out the Muslim Brotherhood for good. Judicial oversight of elections would be replaced by a government-appointed panel and special powers of arrest and eaves-dropping that the police now enjoy under 26-year-old emergency laws would be formally enshrined in the constitution. Small wonder that Egypt's secular and religious opposition, in a rare show of unity, have joined in condemning the reforms as a sham.

The pattern of regression is similar elsewhere. After long debate, Jordan's parliament has approved a press law that allows journalists to be jailed for vaguely defined forms of slander. Similar laws have led to lengthy sentences for journalists in Yemen and Algeria as well as internet bloggers in Tunisia and Egypt. Last month, Saudi Arabia arrested ten intellectuals for signing a polite petition suggesting it was time for the kingdom to consider a transition to constitutional monarchy.

Darker dictatorships, such as those in Syria and Libya, never offered much hope of change in the first place, and continue to silence dissent with gusto. But countries that seemed to offer brighter prospects have also disappointed. Bahrain, a small, relatively progressive island kingdom in the Gulf, had promised that last November's legislative elections would herald a new era of trust between the disgruntled Shia majority and the ruling family's Sunni allies. But electoral rules again diluted Shia votes; with opposition activists facing renewed harassment since the voting, unrest has again spread. People-power in Lebanon, the most politically open Arab country, did succeed in installing a reform-minded government. But subsequent turmoil, including last summer's war that Hizbullah sparked with Israel, has produced such severe political polarisation that many Lebanese fear the country is sliding away from the rule of law and

back into the vicious tribalism of its 1975-90 civil war.

Given the messy outcomes produced by more open politics in Iraq, Palestine and Lebanon, the region's stability-obsessed regimes have had reason to take pause. Yet they are not the only ones to have developed cold feet. Despite the fact that America's State Department, in its recently released annual report on human rights, contained harsh words about American allies such as Saudi Arabia and Jordan, the tone of America's rhetoric about democratisation has grown markedly milder of late. Worried more by the Iraqi quagmire, the perceived threat of Iran and evidence of increased support for Islamist parties that are assumed to be hostile to the West, American diplomacy appears to have dropped idealism in favour of realism. Instead of bullying its friends, America has quietly proffered rewards, including, for example, assistance in developing civilian nuclear energy for Egypt and Libya.

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Israel

Better red than dead?

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A plan to save the Dead Sea looks environmentally and economically dubious

THE Dead Sea, famous for its therapeutic minerals and for the way people float in it like corks, is evaporating away, its surface level dropping by nearly one metre a year. Fresh water from the Jordan river replenishes it at less than one-twentieth the rate of a few decades ago; the rest goes to growing populations of Israelis, Jordanians and Palestinians. Studies suggest that the world's lowest body of water won't vanish altogether, but will stabilise at about 100m lower than it is now. That spells disaster for the environment, and for the tourist resorts on its shores.

This week Israel's government upgraded the “Peace Corridor”, a plan dreamt up by Shimon Peres, Israel's deputy prime minister, to a “national project”, meaning it will face fewer bureaucratic hurdles. Among other mega-projects (see map), the plan proposes a 200km-long conduit to bring water from the Red Sea, at Israel's southern tip, to the Dead Sea. Some will replenish and stabilise the Dead Sea. The rest will be desalinated, using the energy gained from its downhill run, to supply fresh water to all three peoples.

Mr Peres is pushing this project as part of his vision of peace through economic development. The conduit could cost anything up to $5 billion.

Environmentalists, though, are sceptical. Research by the Geological Survey of Israel suggests that sea brine added to the hyper-salty, denser Dead Sea will float on the surface, mixing in only over years or decades. If so, what draws the tourists in will be lost, and algal blooms could turn the water from blue to reddish-brown.

The economics are also dubious. Red Sea water would have to climb 125m before running downhill to the Dead Sea. Once desalinated, it would have to climb again by up to 1.4km to reach Jordanian, Israeli and

Palestinian cities. The cost of all this pumping, according to one American study, might outweigh the energy gains from the downhill run.

A World Bank feasibility study, due to start this year, should settle these questions. However, among other things it will, according to a copy of the terms of reference seen by *The Economist*, try to factor in an “order of magnitude” value for a mysterious economic quantity called the “peace dividend”, not a typical variable for the World Bank.

The study will also examine whether better water husbandry in the region could keep the Dead Sea alive—something that Friends of the Earth Middle East, an environmental lobby, says nobody has studied properly so far. However, on this, the conclusions seem foregone. “Any potential flow returning to the lower Jordan river will be nowhere near sufficient to stop the fall of the Dead Sea unless we go back to the time of Christ or Moses,” says Vahid Alavian, a World Bank official. And in any case, says an adviser to Mr Peres, the plan's progress is “not dependent” on the World Bank study. So what exactly is the study for?

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Russian politics

The Kremlin's new cookbook

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Peter Schrank

President Vladimir Putin has devised a win-win system of elections

Get article background

SEASON your *shashlik* with onion, pepper, coriander and basil. Then marinate in the fridge for 12 hours, advises Dmitry Kuzmin, mayor of the southern Russian city of Stavropol, and also local leader of the Just Russia party. Posing in their pinafores, Mr Kuzmin and his fellow candidates published a leaflet of their favourite recipes as part of their campaign for the regional elections on March 11th. “Sell the Bentley—pay the alimony”, election posters urged the region's governor, who has had a nasty divorce and is aligned with United Russia, a rival party that dominates both the Duma, the lower house of Russia's parliament, and most of the regions. Trivial and dirty tactics these may be, but they are effective. Just Russia surprisingly topped the poll in Stavropol.

Does that point to a real political fight in Russia? Just Russia's strong showing was hailed by Sergei Mironov, its leader, as “a victory over fear”. But the party was created only last October, and like United Russia, it is sycophantically loyal to the Kremlin in general and to Vladimir Putin in particular. Both parties have the president's blessing and, rather like rival disciples to a prophet, both claim to be his true acolytes. “I support him completely,” says Alexander Babakov, Just Russia's top man in the Duma. Criticising the president, he adds, lies outside the purview of party politics. His party purports to be more social-democratic than United Russia. But in the regions, says Nikolai Petrov of the Carnegie Moscow Centre, the important divides are not ideological but between fractious elites vying for power and assets.

The votes held on March 11th in 14 of Russia's 86 regions (United Russia won in the 13 other than Stavropol) marked the start of a political season that will culminate in elections for the Duma this December and for the presidency next March. They suggested how the Kremlin's election-cooking recipe is likely to turn out: one of fake competition, conducted by candidates who are much less different than they try to seem. Undesirables will be nobbled in advance, by denying them access to state-controlled television, and by new laws on political parties and elections that make it difficult for them to run or to win seats when they do. (The head of Russia's central election commission, a placeman who nevertheless publicly doubted some of the new rules, was ousted from his job this week.)

In St Petersburg, for example, apparently fierce regional campaigning by United Russia and Just Russia generated such ruses as bogus death notices and the circulation of pornographic videos featuring candidate lookalikes. But Yabloko, a liberal party, was kept off the ballot, because (say its leaders) of its opposition to the governor and to Gazprom's plans to build a skyscraper in the city.

Regional governors are unlikely to stray from the Kremlin's plans. The regions have varying levels of autonomy and prosperity, but all their bosses are, in effect, now appointed by the president. The Stavropol result was probably in part a protest against an unpopular governor, whom voters cannot remove directly.

In the Duma elections in December, only four parties look likely to climb over the 7% threshold for seats: Just Russia and United Russia, which seem destined to emerge as the components of a simulated two-party system, plus the Communists and the misnamed Liberal Democrats. The Union of Right Forces, a liberal party that is less troublesome than Yabloko, may also just squeeze in.

As for the presidential election, rather than being a simple anointing of Mr Putin's chosen successor, it may turn out to be a contest between two principal candidates—albeit both approved by the Kremlin. This recipe is likely to work well enough to leave little need for the massive falsification and repression that mark elections in some of Russia's neighbours (although there was a polling day shoot-out last weekend in the Russian republic of Dagestan). But riot police will be available if necessary, as participants at a violently dispersed protest rally in St Petersburg on March 3rd were quick to discover.

“There is no political competition in our country any more,” says Mikhail Kasyanov, a former prime minister turned Kremlin critic, gloomily. To some, the situation is starting to look rather like the old Soviet Union, in which elections also took place. Indeed, in some places, United Russia is now behaving uncannily like the old Communist Party, with applicants for certain jobs required to be members. Even so, a closer analogy is probably with the pre-revolutionary period, when groups of powerful boyars—sort of barons—competed for the tsar's ear and favour. (During the civil war Ivan Bunin, a writer, noted the “extreme repetitiveness” of Russian history, “its fatal peculiarity of always moving forward in circles”.)

A case can be made that this arrangement works quite well. Witness Russia's economic progress under Mr Putin, and his still-stellar popularity—even if that is attributable in part to the Kremlin's media management, and to the widespread political quietism that followed Russia's stressful 1990s. Elections may be closed and phoney, but Russia's rulers are responsive to the popular mood in their own way, as in the nervous backtracking that followed big street protests against a reform of the benefits system in 2005.

But there are risks in a situation in which all politicians owe their positions to the Kremlin, not to the voters. Many of those voters continue to suffer horrifically from Russia's widespread poverty and inequality, which may explain the enduring appeal of the Communists, who came second by share of the vote in last week's polls. (Mr Babakov says they are not real communists but “just a group of people who are exploiting the brand”.) Add to this a catastrophic demographic collapse, mind-boggling corruption and a bloody crisis in Chechnya that may look solved but isn't. After Mr Putin leaves office, especially if the oil price falls and the material gains of his presidency fade away, ever more Russians may become frustrated with rulers who offer them recipes for *shashlik* but not for genuine change.

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Spain and terrorism

Zapatero's dilemmas

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The issue of terrorism returns to the heart of Spanish politics

AFP

A plazaful of protesters

IT WAS a difficult call. Spain's Socialist prime minister, José Luis Rodríguez Zapatero, could have let Iñaki De Juana, an imprisoned member of the Basque separatist group ETA, die on hunger strike. But that would destroy any short-term hopes of ETA laying down its arms. Or he could have sent the prisoner home under house arrest to serve out the last part of a three-year sentence for making terrorist threats. That would anger not just the opposition People's Party (PP), but most Spaniards.

In the event Mr Zapatero chose the second course. Was this cowardly, foolish—or brave? Most Spaniards incline to the first two adjectives. Polls say that 59% wanted Mr De Juana kept under lock and key. Few cared if he became a separatist martyr.

Mr De Juana, who had previously served a long prison term for 25 killings, is now in the comfort of a hospital bed in the Basque country and will soon go home. But Mr Zapatero is suffering. His poll ratings have plummeted. The De Juana affair has proved to be a political gift for the PP leader, Mariano Rajoy. He drew several hundred thousand people to Madrid on March 10th to parade behind banners proclaiming “No more concessions to ETA”.

Even more ominously for Mr Zapatero, the De Juana decision has put terrorism at the centre of Spanish politics. That is what the PP has wanted since March 11th 2004, when bombs planted by Islamist terrorists killed 191 people on four trains in Madrid. Three days later voters threw the PP out of power in a general election. The PP has spent the past three years fanning improbable conspiracy theories about the train bombings, most of which are based on the notion that ETA was somehow involved.

Mr Zapatero, these conspiracy theorists claim, is trying to cover up the facts. Yet the current trial of 29 mainly Muslim men suspected of involvement in the bombings has turned up no ETA connection. The police also insist that they have found nothing. Opinion polls nevertheless show that fully a third of Spaniards mistrust the official version.

Terrorism is now drowning out most other political debate. The PP's anti-ETA message is being heard loud and clear; its calls for economic liberalisation barely make a mark. Mr Zapatero's decision to release Mr De Juana has similarly stopped Spaniards from taking in the news that the economy racked up 3.9% growth in 2006, the fastest since 2000.

With the dead from the train bombings and from four decades of ETA violence at the heart of such an emotive debate, the political temperature in Spain is rising. For some it is already too hot. Even the survivors of terrorism and the relatives of the dead are divided. Most train-bomb victims disavow the PP's attempts to blame ETA. Most ETA victims dislike Mr Zapatero's attempts to talk peace. Both groups are trundled out by the political parties to argue their cases. Several have had enough. “Who is going to smooth away the pain that is being added to our existing pain?” demanded Pilar Manjón, head of an association of train-bomb victims, on March 11th, as a monument was unveiled at a tense ceremony to mark the third anniversary of the 2004 attacks.

It is dismaying that ETA now finds it so easy to set Spain's political agenda. A much-weakened group that has killed only four people in the past four years (compared with 800 in the previous 36) now exerts an influence that far outweighs its capacity for violence. The De Juana case was the second big test of Mr Zapatero's resolve to talk peace. ETA had already tried him in December, when it broke a nine-month-old ceasefire by exploding a car bomb at Madrid airport, killing two Ecuadoreans. Even so, it has been claiming that the ceasefire remains in place.

Now Mr Zapatero must decide whether to allow ETA's banned political wing, Batasuna, to rename itself and stand in May's local elections. Saying yes could keep the Basque peace process shakily on track. But Mr Zapatero has said that Batasuna must first explicitly renounce all support for violence. He is no longer in a strong enough position to take more risks.

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Reinventing Hamburg

Hanseatic realpolitik

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A city always ready for the next deal

AN UNUSUAL piece of sabotage recently stopped Mathias Petersen, three of whose forebears were mayors of Hamburg, from following in their footsteps. During voting to choose a Social Democratic (SPD) mayoral candidate, some 1,000 ballot papers were stolen. The local party leadership resigned in disgrace—and Mr Petersen and his rival, Dorothee Stapelfeldt, both chose not to run again.

This may be sad for history—his great-great-grandfather, Carl Friedrich Petersen, laid the cornerstone of the *Rathaus* in 1886—but it will not blight Hamburg's future. On March 7th Michael Naumann stood down as publisher of *Die Zeit*, a weekly, to be the SPD's candidate. Recent mayors, right or left, have all focused on reviving jobs and commerce in what was once continental Europe's greatest trading city, but which has fallen on hard times despite Germany's export boom.

Hamburg has not fought shy of public intervention to help itself. Several times in the past 30 years, its Senate has stepped in with money to save firms from closure or foreign takeover—more often than not coming out with a profit. So it was with Messerschmitt-Bölkow-Blohm, a local aircraft-maker, saved in 1976 and sold on to Daimler in 1989 (this became Daimler's stake in EADS, builder of Airbus, which employs 12,000 in Hamburg but is now set to shed jobs). Or with Beiersdorf, maker of Nivea cream, which was saved from takeover and possible break-up in 2003, when Tchibo, a family-owned coffee group also based in Hamburg, was persuaded to increase its stake. The city also took a stake that it has just sold for a small profit “over and above the tax revenues and the jobs we secured”, says Gunnar Uldall, economics minister in the centre-right Christian Democrat (CDU) government.

Job creation is Mr Uldall's biggest goal. To achieve it the city must go for more growth and more trade. That has meant battling with environmentalists to extend the airport's runway into some hallowed wetlands, so that the freighter version of the new Airbus 380 can be built and flown there (though now the project is on hold). Earlier this year the city won a court battle to evict protesters from a small plot of land they had bought to obstruct the extension.

There are similar plans to expand Hamburg's port, which has hopes of overtaking Rotterdam as Europe's biggest container port. Last November the city invited outside investors to take a 49.9% stake in the city-owned HHLA (Hamburger Hafen & Logistik), which handles two-thirds of the freight passing through the port. This week it decided to float some 30% of HHLA in a public offering instead. The city will use the proceeds to pay for the expansion of the port, with the aim of doubling its capacity by 2015.

Besides its harbour, aircraft-making, coffee and cosmetics, Hamburg is also Germany's media capital. Its three big publishing houses, Gruner + Jahr, Bauer and Spiegel, command about 50% of the German print market; two leading weeklies, *Die Zeit* and *Der Spiegel*, are based in Hamburg. The city hosts a string of film and broadcasting companies. Suggestions that the media might follow the government to Berlin have so far proved wrong.

Cleverly drawn maps show Hamburg as a natural gateway to central Europe and the Baltic. The city has historical links with China and the rest of Asia. Deutsche Bahn, the German rail group, had plans to run its logistics from Hamburg and to invest in HHLA, but it has now dropped them.

This was a rare setback for Otto Gellert, a Hamburg veteran who advised Deutsche Bahn. He did some of the city's biggest deals, including MBB, Beiersdorf and the sale of Reemtsma to Imperial Tobacco in 2002. He once had a stake in M.M. Warburg, a local investment bank, and was deputy chairman of the *Treuhandanstalt*, the agency for privatisation in the old East Germany. Next week he will submit a bid to return Hamburg's best-known hotel, the Vier Jahreszeiten (Four Seasons) from foreign to local ownership. This old Hanseatic town has plenty of new ambitions.

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Churches in eastern Europe

God-bothered

Mar 15th 2007 | BUCHAREST, PRAGUE AND WARSAW
From The Economist print edition

Religion in central and eastern Europe is waning—and plagued by scandal

PERSECUTED, valiant and victorious. That was how the churches of eastern Europe seemed in 1989. It was a flattering picture. In truth, totalitarianism spawned heroism, treachery and corruption in the church, as in other parts of life. It also stunted thinking on ecumenism and tolerance. Now secularism is shrivelling some churches, especially mainstream Protestant ones. Others have retreated into steamy nationalist ghettos, sometimes in cahoots with the new authorities. Everywhere disturbing, long-hidden questions are emerging about collaboration with the communists. It is not an uplifting picture.

Religious freedom is still an issue. Nothing matches the persecution of believers in such totalitarian places as Belarus or Turkmenistan. But minority denominations face tiresome legal obstacles, especially in countries with big traditional churches. Romania's new religion law, rushed through parliament last year, requires 12 years' existence and 22,000 members for full registration. Churches with fewer than 300 members are not allowed to own property or have paid employees. The law bolsters the majority Romanian Orthodox Church, freeing it from legal challenges over communist-era property seizures from rival churches (when, as now, it worked closely with the state). Opponents plan to challenge the law in the European Court of Human Rights.

Elsewhere in the Balkans the story is similar, especially in places where (as in England, Denmark and Norway) a “national church” enjoys power underpinned by the state. Macedonia's authorities protect the local Orthodox church from its Serbian neighbour, whose priests, seen by patriotic Macedonians as agents of Serbia, may not cross the border wearing clerical garb. “The sort of thing you would expect in Turkey,” sniffs Felix Corley of Forum 18, a religious-freedom watchdog. The Serbian Orthodox archbishop in Macedonia has been jailed twice: once for publishing a calendar that challenged the Macedonian hierarchy's view of church affairs and “causing national, racial and religious hatred and intolerance”; the second time for embezzlement of church funds.

Meanwhile the Serbian Orthodox monasteries of Kosovo—where a couple of dozen churches were wrecked or damaged by ethnic Albanians in 2004—are watching talks on the province's political future nervously. This week monks at the medieval monastery of Decani were urging NATO's supreme commander, General John Craddock, to continue protecting them if and when Kosovo becomes an independent, Albanian-dominated state.

Then there is politics. In some places, the church hits a resonant, non-partisan note. A Lithuanian archbishop, Sigitas Tamkevicius, who spent five years in the Soviet *gulag*, is an ardent and widely admired proponent of reconciliation between victims and perpetrators of communist crimes. Elsewhere, the church's involvement is more controversial. In Poland, where 90% of the population say they are Catholic, the ruling coalition displays ostentatious religiosity. The speaker of parliament crosses himself before taking his seat. Government supporters depict the opposition, ex-communists and liberal conservatives, as heathen secular liberals—by implication, not proper Poles.

Yet all is not what it seems. The church in Poland is divided between Vatican loyalists, who often oppose close involvement in politics, and energetic dissidents linked to Radio Maryja, a hardline broadcaster. This once had huge clout, articulating the feelings of Poles alienated by the country's brisk, materialist business culture and the decay in moral norms. But Radio Maryja's audience has shrunk in the past decade to no more than 2% of all current listeners. Voters who wanted a clean sweep and a new moral order have found that, although their favourite parties are in power, disappointingly little has changed.

Faith in the church's integrity has also been damaged by allegations that Stanislaw Wielgus, who stepped down as archbishop-designate of Warsaw, once co-operated with the communist secret services. Some sense a witch-hunt. Others welcome the breaking of a taboo. A new book based on secret-police records

in Cracow claims 30 clergy and four bishops collaborated; some of those named deny it.

There are similar worries for the Catholic church in the Czech Republic and Slovakia. Cardinal Miloslav Vlk, the Czech primate, has called for clergy to be screened for co-operation with the secret police. But in most places involvement in politics is waning. On the burning moral issues of today, such as integrity in politics, public-spiritedness, honesty about history and compassion for the unfortunate, the churches seem to have little to say.

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Silvio Berlusconi in court again

Justice on trial

Mar 15th 2007 | MILAN
From The Economist print edition

Why it is so hard to convict anybody in Italy

WHEN the long-awaited corruption trial of Silvio Berlusconi, Italy's former prime minister, and his former lawyer, David Mills, the estranged husband of Tessa Jowell, a British cabinet minister, opened on March 13th, the courtroom in Milan was packed. Eighteen judges, lawyers and clerks were there, with a trolley full of dog-eared folders and documents. Yet in the four hours of legal argument that followed, nobody gave even a hint that what they were all doing was essentially futile.

Because of legislation introduced when Mr Berlusconi was prime minister, his trial, plus the two appeals allowed under Italian law, have to be completed by next February. Otherwise the case automatically lapses under Italy's statute of limitations.

Giuseppe Gennaro, president of the Italian national magistrates' association, says that the entire judicial process takes more than eight years on average. It is highly unlikely that the case against Mr Berlusconi and Mr Mills will be dispatched in 11 months. Trials in Italy do not even take place continuously. In this case, the earliest day on which the protagonists could attend a second hearing was March 22nd, but a lawyers' strike is due to take place that day.

The trial of Mr Berlusconi and Mr Mills, in which the defendants deny giving and receiving a $600,000 bribe, offers an insight into the surreal world of Italian justice. For the statute of limitations, which makes it almost impossible for prosecutors to convict anybody of white-collar crimes, is not the only problem.

After Mr Berlusconi left office, parliament granted a partial amnesty that reduced by three years the sentences for any offences committed before the statute came into effect (not just those that had already been tried). The government said this measure was necessary to clear out the jails; some 26,000 prisoners have since been freed. But for the first time since 1948, the amnesty was not accompanied by a pardon (extinguishing the offences themselves).

For untried offences, says Mr Gennaro, “this means that it is necessary to hold the trial and at the end, in the event of a guilty verdict, pass a sentence that cannot be carried out.” Since Italian justice moves so slowly, most cases before the courts now concern offences committed before the amnesty. A report by a body overseeing the judiciary concluded last year that over 90% of trials in the next five years could be pointless.

Prosecutors in Italy are answerable only to their immediate superiors. Some have grasped the amnesty as a chance to reduce their backlog of work by shelving cases that cannot result in a sentence. Others, including the prosecutors in the Berlusconi and Mills case, have taken the purist view that they should not pick and choose. “They may feel they don't have the authority to decide,” says Mr Gennaro, the palms of his hands upturned in a gesture of resignation. In any event, Mr Berlusconi and Mr Mills are in no real danger of going to jail.

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Charlemagne

Climate control

Mar 15th 2007
From The Economist print edition

The European Union thinks it can be a model for the world on climate change. Can it?

Peter Schrank

TO EUROPEANS, climate change embodies all the trends that will make the European Union exemplary in the next 50 years. The future, they think, will be all about solving global problems by pooling sovereignty and setting up a framework of mutually accepted rules. This will be as true for trade and conflict resolution as it is for environmental policy.

Hence the significance of last week's summit deal on reducing greenhouse gases. In a recent podcast Angela Merkel, Germany's chancellor, celebrates the example that Europe is setting. Having persuaded the EU to do more to cut emissions, she claims she will now have the moral authority to cajole America, India and China into following suit, starting at another international jamboree over which she will preside: a summit of the G8 club of rich countries in June. Tony Blair and Jacques Chirac chime in that Europe has seized the environmental high ground. José Manuel Barroso, the president of the European Commission, believes the deal means that Europe now leads the world in combating climate change.

The summit certainly set some ambitious goals. The 27 members of the EU pledged to reduce their greenhouse-gas emissions by at least 20% from their 1990 level by 2020. They promised to deepen the cut to 30%, if other rich countries joined in. The goal is to be met by a variety of smaller schemes: increasing the share of energy that comes from renewable sources such as sunlight and wind to 20%, making 10% of transport fuel from plants, improving energy efficiency by 20%, and so on.

Setting fixed targets serves two purposes. First, it provides companies with a clearer view of their future obligations. Before the agreement was unveiled, they could see only as far as 2012—the expiry date of the Kyoto protocol, the United Nations' treaty on climate change. Now they know that polluting will become ever more costly until at least 2020, and can plan their investments accordingly. Second, as Mrs Merkel suggested, the EU's plan may act as a spur to less high-minded countries like America, encourage green lobbyists to put more pressure on governments everywhere and provide a starting-point for negotiations about what should replace Kyoto.

Both ideas are laudable. Unfortunately, the EU often seems more committed to grand statements of intent than to practical steps to achieve their aims. Consider the emissions-trading scheme (ETS), Europe's flagship programme for reducing greenhouse gases. Under the ETS, companies get a fixed number of permits to pollute. As they grow, they must either reduce emissions or buy spare permits from other firms that have done more to clean up their act. Such “cap-and-trade” schemes have proved a cheap and

effective way to reduce emissions of other pollutants in America. But the EU handed out too many permits for the ETS, resulting in little if any reduction in emissions. Worse, governments handed out the permits free, in effect rewarding the dirtiest firms with a valuable asset.

Mr Barroso's underlings at the European Commission are now scrambling to fix these faults. Arnold Schwarzenegger, governor of California, has expressed polite interest in the ETS. But for American states devising cap-and-trade programmes of their own, it has been as much a cautionary tale as a role model.

The new initiatives championed by Mrs Merkel might just add to the embarrassment. The EU's politicians are not only telling businesses to cut emissions, but also dictating how they should do it (rather like communist central planning, muttered the Czech prime minister, accurately). There is a big emphasis on wind and solar power, even though the latter costs more than other low-carbon alternatives, such as nuclear power. The EU is planning to offer incentives to businesses that can somehow capture and store their own emissions, even though the technology involved remains unproven. Nobody knows how much any of this will cost.

It would be far better to stick to repairing and expanding the ETS, and let businesses and consumers decide for themselves the best way to comply. That would be economically rational. But it would also deprive leaders of the opportunity of handing out largesse in the name of greenery.

Greener than thou

The targets may have a practical purpose; but they also need to be met. The EU's credibility as a role model rather depends on it. But Europeans have a bad habit of missing their own targets. All 27 EU members signed up to Kyoto, but most have not cut their own greenhouses gases enough to meet their targets, so they will have to pay for equivalent reductions in poor countries instead. Only two reached the prescribed 2% mix of biofuels in their petrol and diesel consumption by 2005. The same thing could happen now. Indeed, the summiteers all but admitted that they would not reach the new targets when they acknowledged that countries such as Poland and Slovakia would not be able to produce the prescribed amount of renewable energy. Instead, the EU said, the goals would be met on average across the club as a whole. Yet it is hard to imagine that there are countries so virtuous that they will be greener than required, presumably at great expense, just so that their neighbours can continue to be grubby.

Such flaws mean Europeans now risk disappointment both on climate change and on their union's leadership role. On climate change, the EU is a small part of the problem (its members produce only a seventh of world carbon pollution). But they hope to be a big part of the solution. There is a mismatch.

And that will have an impact on the EU. The EU has embraced greenery partly from conviction, partly to give itself a role in the world. Europe will rescue the environment from destruction; the environment will rescue Europe from irrelevance. But the EU would be a lot more relevant if its policies made better economic sense.

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Correction: Special report on the European Union

Mar 15th 2007
From The Economist print edition

In some copies of this week's special report on the European Union, table 7 in the penultimate article incorrectly puts Sweden in NATO, and fails to list Portugal as being in Schengen. Sorry. This error has been corrected online.

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Climate change

A hot topic gets hotter

Mar 15th 2007
From The Economist print edition

David Simonds

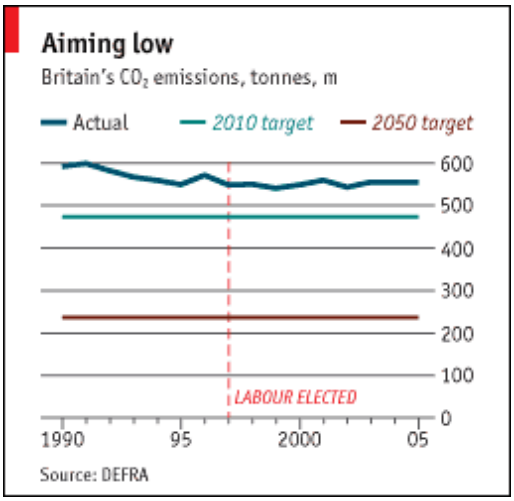
Politicians are competing to see who can be most eco-friendly, but the public may not be as enthusiastic as they suppose

Get article background

FREE-MARKETEERS have long argued that competition improves products and services. If they are right, Britain is on its way to having the best climate-change policy in the world. This week David Cameron, the Tory leader, and Gordon Brown, the chancellor and Labour's leader-in-waiting, clashed head-on as each brandished claims to be the more ostentatiously and radically green.

The spur was the publication, on March 13th, of the government's climate-change bill. Britain has longed fancied itself a world leader on the matter. It is on track to meet its obligation under the Kyoto protocol to reduce greenhouse-gas emissions by 12.5%, compared with 1990 levels, by 2008-12. Indeed, so confident were ministers that in 2003 they set themselves two voluntary targets alongside their Kyoto obligation—to cut emissions of carbon dioxide (the main greenhouse gas) by 20% by 2010, and by 60% by 2050.

That looked ambitious at the time. Now, with only three years until the first target must be met, even the government admits it is unlikely to be (see chart). Stung by criticism that their apocalyptic rhetoric (Tony Blair describes climate change as “the greatest challenge facing humanity”) was so much hot air, ministers last year promised a fresh approach.



The new bill, expected to be law by next year, aims to elevate the 2050 target from a voluntary aspiration to a legally binding obligation. It proposes a system of “carbon budgets”—rolling five-year limits on carbon-dioxide emissions, planned 15 years in advance. An independent Committee on Climate Change will advise ministers on how to meet their aims and give annual reports to Parliament. Fired with radical spirit, David Miliband, the environment secretary, said that his bill was “the first of its kind in any country,” although the French have had something similar

since 2005. Even Mr Brown, not known as a tree-hugger, seized
the chance to buff his green credentials in two speeches. On March 13th he called for a “new world order” to sort out the climate and for more co-operation within the European Union (which has recently agreed to carbon cuts for all its member states).

Indeed, climate change has become as much a political battleground as health, education or immigration (see article). On March 12th Mr Cameron—author of his party's arboreal new logo—made his own assault on the moral high ground. In a speech in London he rubbished Labour's environmental record, pointing out, correctly, that carbon dioxide emissions are higher now than when the Labour Party came to power.

Some of the Tory leader's proposals were uncontroversial: he called for improvements to the EU's emissions-trading scheme (which allows carbon-heavy firms to buy emissions permits from cleaner ones). Others were bolder: he suggested personal aviation-mileage allowances that could be exceeded only by paying progressively higher taxes, as well as annual national targets for carbon reduction, something the government has sensibly rejected as being too rigid. This puts the Tories in unfamiliar company: Friends of the Earth, for example, an eco-lobbying outfit, also supports annual reductions. Mr Cameron was able to call on some high-wattage publicity by revealing that Al Gore, once America's vice-president and now the world's best-known climate-change campaigner, was to address the party's front bench—quite a coup, given that Mr Gore's Democratic Party has traditional links with Labour.

But the crusading spirit has not reached every corner of society. Some question how committed ministers really are, since the bill is unclear about what sanctions will apply if targets are missed. Business views are mixed: the Confederation of British Industry is broadly happy, but the Engineering Employers' Federation, which represents industrial firms, worries about the bill's effects on competitiveness.

The ever-greater predominance of climate change in public discourse may be making dissenting voices shriller. Lord Lawson, a former chancellor, has cast public doubt on whether man-made greenhouse-gas emissions really warm the planet. The Centre for Policy Studies, a right-wing think-tank, produced a pamphlet to the same effect earlier this month. And last week Channel 4, a commercial-television station, broadcast a documentary arguing that the sun, not mankind, was to blame for climate change.

Critics point out that the arguments used are flatly untrue or misleading, or else ignore recent evidence. Carl Wunsch, an oceanographer at the Massachusetts Institute of Technology, has complained that the way his views were portrayed in the programme “comes close to fraud”. Martin Durkin, the programme's director, has engaged in similar shenanigans before. In 1998 Channel 4 had to apologise after another of his documentaries was found to have distorted contributors' views. Most of the talking points are imported from America, where contrarian views on climate change have a long pedigree.

Pinning down public opinion amid all this sound and fury is tricky. Greens like to point to polls in which people say they would happily pay higher taxes on environmentally unfriendly things such as jet travel and large cars, or to buoyant sales of rooftop wind turbines, as proof that the public has been converted. But Peter Kellner, the boss of YouGov, a polling firm, counsels caution. “The public is convinced about the science of climate change,” he says. “But most of the things they're willing to do are ones that are either easy or that other people pay for.”

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Carbon offsets

Ripping off would-be greens?

Mar 15th 2007
From The Economist print edition

A rapidly growing market is attracting some timely scrutiny

Get article background

ONCE the workshop of the world, Britain is fast mastering an entirely post-industrial art—that of turning something into nothing. As anxiety about climate change grows, the business of selling emissions offsets is increasing along with it. A recent poll by TNS for Halifax, a bank, found that a tenth of Britons would consider paying to offset the greenhouse gases they generate while flying on holiday. And at least 14 British companies—twice as many such firms as any other country has produced—are busily collecting money from conscientious travellers and other concerned individuals as well as firms. They promise to make the offending carbon dioxide disappear from thin air by, for instance, planting trees that will suck it in or cutting other people's emissions elsewhere. The Carbon Trust, funded by the British government, reckons that the market for these offsets is growing by 60% a year in Britain.

This should be welcome news, because voluntary offsets, while small at the moment, can in time help to slow global warming. But many fret that the nascent industry may be harmed by the sharp practices of some of its operators.

Britain's environment department, DEFRA, says one problem is that offset providers use different methods of calculating emissions. This is because there are disagreements over exactly how they should be counted, given that an aeroplane's emissions per passenger will vary depending on factors ranging from how full it is to the weather. But the result is that passengers who want to neutralise the impact of identical flights may be given widely differing estimates by different firms of the size of the offset required. Nor do firms use the same ready reckoner in calculating just how much carbon planting a tree soaks up. This variability is reflected in the price of voluntary offsets, which range from €2 ($2.65) to €30 per tonne of carbon dioxide.

Moreover, many of the methods used to create offsets are dubious. A study by Stefan Gossling, of Lund University in Sweden, found that three-quarters of firms selling voluntary offsets base them on forestry. Yet this way of sequestering carbon is controversial. Trees may wither and die before absorbing much CO_2, and will in time decay, releasing it back into the atmosphere.

Efforts are now being made to clean up this murky market. Industry groups are drawing up voluntary standards, some stricter than others. But a profusion of benchmarks may just confuse consumers. DEFRA reckons a single standard could create fungible offsets and provide transparent pricing.

But regulation poses its own dangers. Voluntary-offset firms have prospered because they are able to produce emissions reductions more cheaply, and often more imaginatively, than those that are bound up in the red tape of the Kyoto process, for example. Regulation that is too heavy-handed could stifle a flourishing business.

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The Olympic bill

Record-breaking

Mar 15th 2007
From The Economist print edition

The government has got its sums badly wrong. Who should pay?

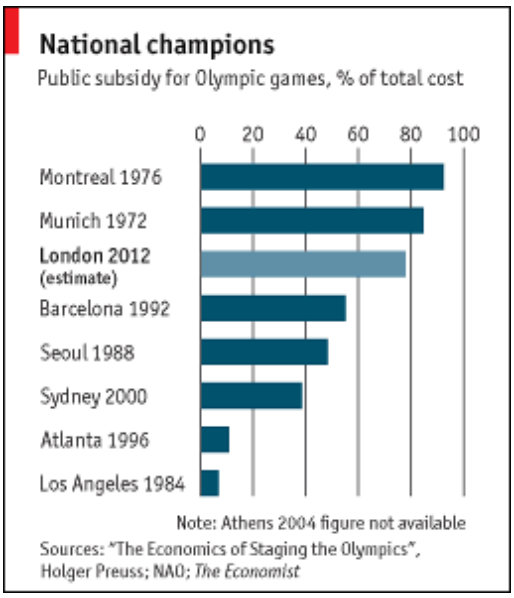
"FASTER, higher, stronger," goes the official Olympic motto. Plenty of alternative adjectives are beginning to spring to mind. The original plan for London's games, agreed upon in 2003, put the public cost of organising and staging the month-long spectacular at £2.4 billion ($4.6 billion). Private investment, plus revenue from tickets and the like, would raise another £2.2 billion. A further £1 billion in "regeneration" infrastructure upgrades, already pencilled in by the Treasury, would be brought forward for the 2012 deadline.

On March 15th Tessa Jowell, the culture secretary, made a long-expected admission that the real bill would bear little relation to those figures. With five years to go and the builders yet to lay a brick, she revealed that the full cost will be more than £9 billion. The central government's share has risen to more than £6 billion, she said, due mainly to rising construction costs, consultancy fees and a supposedly unforeseen tax bill. Security, first budgeted at £190m, has become far pricier since the terrorist attacks of July 2005; it is now likely to cost £600m more than before. And a contingency fund of £2.7 billion has been added in case the new estimates prove no more reliable than the old ones.

Every Olympic venture faces critics, most memorably the "People Ingeniously Subverting the Sydney Olympic Farce" (PISSOF). But governments are keener than ever to host the show: Los Angeles was the only city willing to do the honours in 1984, whereas London had to fend off eight rivals. At least a dozen countries are mulling bids for 2016. Why take on such an expensive lot of bother?

In fact, as the chart shows, vast public works are not essential. In Los Angeles and Atlanta the city authorities voted to spend next to nothing on new building, relying instead on existing venues and putting up athletes in student halls. Both games made a small profit—in contrast to Montreal, which splashed out on a new Olympic park in 1976. Its citizens paid off their debts only last year.

Rather than run cheap and cheerful games, paid for with revenue from television rights, sponsorship and tickets, London has chosen to splurge. The London Organising Committee, whose job it is to run the event itself, expects to cover its own costs, estimated today at £2 billion; the charge to the public comes almost entirely from new stadiums and infrastructure. On the revised budget, the London Olympics will be among the most heavily subsidised in recent history.



Behind the scenes there has been epic wrangling over who should pay. The spectre of Montreal looms: its unlucky citizens faced ruin because Canada's government avoided financial liability, leaving the city to meet its costs alone. In Britain, the central government has been more generous. But Londoners, who are already contributing £625m over ten years through an increase in property tax, will now be asked for more. London's mayor, Ken Livingstone, has promised not to raise the Olympic tax. Not everyone believed this at the time, and perhaps rightly: it now emerges that he is going to have to find another £300m somehow or other. Yet the Treasury is not keen to foot the rest; there is still a shortfall of almost £700m. What to do?

Enter the National Lottery, a gigantic, helpless slush fund that the government is never reluctant to abuse. Already £410m is being diverted to the Olympics from other good causes, and a set of "Olympic" lottery

games will raise another £750m (Camelot, the lottery's operators, estimate that three-quarters of these sales will be cannibalised from the normal lottery). Conveniently, the lottery's grant-giving bodies ultimately answer to Ms Jowell, who has decreed that they must give up another £675m. Pretty unsporting.

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Trident

Rebels with a cause

Mar 15th 2007
From The Economist print edition

Britain's nuclear deterrent is renewed, but only with Conservative support

THE Labour Party has always been an unruly creature, but it is at its most truculent when called to vote on buying guns and fighting wars. The first Labour rebellion in the House of Commons took place in 1924, when Herbert Dunnico voted against Trident, a programme to build fast, light warships. On March 14th Labour MPs followed in his footsteps, voting against Trident in its latest incarnation as Britain's strategic nuclear-weapons system. Compared with the 139 who opposed the Iraq war in 2003, the 95 who said no this time were the parliamentary equivalent of spectators at the back of the cinema throwing popcorn at those in the front. Even so, it was the largest rebellion of this parliament. The issue was divisive enough to prompt four junior members of the government to resign.

Despite the rebels on its own backbenches, the government never risked losing the vote. David Cameron, the Conservative leader, put a three-line whip on his members—the strongest arm-lock available—to back the government. Mr Cameron is currently in a mood to boss his party around, and his lead in the opinion polls gives him the authority to do so: last week he dismissed his homeland-security spokesman, Patrick Mercer, for making racist remarks (which were in fact more ill-judged than prejudiced). Few Conservatives leapt to Mr Mercer's defence.

Mr Cameron's support was a relief for Tony Blair and his likely successor, Gordon Brown, the chancellor, both of whom once favoured unilateral nuclear disarmament. Labour leaders have been tussling with their own party over nuclear weapons ever since the first marches against the bomb in the 1950s. But the government failed to convince its party on either of the two questions put before the Commons: whether Britain should retain a nuclear deterrent; and whether the government needed to make a decision now.

On the first question, the government said that the principle of nuclear deterrence—that states would be rational enough not to launch a nuclear attack on Britain for fear of a nuclear response—still held. But then Des Browne, the defence secretary, asserted that the danger might now lie with rogue states and terrorists unwilling to abide by these rules. When pressed on the circumstances in which Britain might launch nuclear missiles, Mr Browne responded that such uncertainty was a vital part of the deterrent. But 88 Labour MPs voted against him.

On timing, and whether the decision had to be taken now, the government lost 95 Labour votes. The Vanguard-class submarines which carry the missiles with nuclear warheads will be reaching the end of their lives by 2024. The government said they could not be extended, as the Americans are doing to their differently designed subs. It reckoned replacements would take 17 years to design and build. Critics pointed out that the existing ones required only 14 years; but this time the machines would be more complicated, ministers said. If a decision were not taken now, the capacity and know-how to build them would be lost. And so on.

There are two other arguments for Trident. No government wants to risk losing Britain's seat on the UN Security Council, which giving up nuclear weapons might entail. And Trident is a good bargaining chip that should be given up, if at all, in exchange for disarmament elsewhere. But the government did not make them. And the rebels, who thought they had Labour's history and election manifesto (which talks of maintaining Trident rather than renewing it) on their side, felt emboldened.

For Mr Blair this was a minor inconvenience; but for Mr Brown it spells further trouble. The party, says Philip Cowley, of Nottingham University, is growing so used to rebelling that, after a short honeymoon when the chancellor takes over, it is likely to go back to its unruly ways.

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Party funding

Please review your review

Mar 15th 2007
From The Economist print edition

Why a year-long review of financing for political parties will go nowhere fast

BACK in the days before the police began dropping in to 10 Downing Street for chats with the prime minister, Sir Hayden Phillips, a smooth civil servant, was asked to review the funding of political parties. The main ones' finances were in a mess induced by heavy spending in the previous year's general election. Could Sir Hayden find a way to fund them that took account of the long-term decline in party membership and did not leave them in hock to a small number of wealthy donors?

The solution he came up with on March 15th—more state funding, in exchange for tighter fundraising and spending limits—now sounds even more attractive (to the parties at least) than it did a year ago, thanks to the ever-swelling stream of revelations about what has come to be called the cash-for-honours affair. Nobody has been charged yet, and indeed it is becoming hard to remember what the original sin was. Parties have rewarded their backers with peerages for ages. But a year of headlines about skulduggery at the top of the Labour Party has added to the sense that the current set-up is irredeemably corrupt, and that something must be done.

Sir Hayden's recommendations are to remove some of the money from politics by lowering the cap on election spending and limiting the size of donations, to £50,000 apiece. He also suggests reducing the amount each party can spend campaigning in a particular constituency. In return the state would increase the money it gives parties now, doling out the extra cash in proportion to their success in elections and in recruiting paying members.

Though some of these ideas sound sensible, Sir Hayden has tried in vain to forge a consensus in favour of them. The proposals may diminish Labour's most dependable revenue source—donations from the trades unions—just when other sources of funds have deserted the party. For the Conservatives, the limits on spending in target constituencies would rule out repeating one of its few good campaign strategies at the last election, when Lord Ashcroft, a former party treasurer, channelled his own money into close fights rather than giving to Conservative central office. Further negotiations on the basis of these proposals are expected.

Even if they lead nowhere, the question of how politics should be financed will not go away. Democracies seem to need parties. Silvio Berlusconi, the former prime minister of Italy, created his Forza Italia out of thin air but he is not, perhaps, the best model. If there is a public good in maintaining parties, then it may not be unreasonable to ask the taxpayer to step in.

But parties' fortunes are not fixed. Being Democratic or Republican in America aroused fewer passions in the mid-1970s, when the parties agreed on rather a lot. Then the culture wars put them at each others' throats. State funding for mainstream parties in Britain was last increased in 1975, after a period when, as now, Labour and the Tories were hard to tell apart. Then Thatcherism and the Social Democrats invaded the scene. The current consensus may by nature be temporary too, but bigger state subsidies might well prolong it. It seems a dubious use of taxpayers' money to limit their choice as voters.

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Eurovision song contest

Battle of the exes

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A new staging post on the celebrity career path

IT IS less than six months since glam-rocker Justin Hawkins put away his skin-tight lycra catsuit and sparkly platform boots for a spell in rehab. Now, before any but the keenest fans of his erstwhile band, The Darkness, had noticed he was gone, he is staging a comeback. Together with his friend Beverlei Brown, a backing singer, he is competing on March 17th to represent Britain at the Eurovision song contest in May.

The Eurovision is usually a chance for hopefuls to hog the limelight. But this time only one contestant, a singer called Cyndi, is taking a first shot at fame.

Mr Hawkins is also up against Brian Harvey, the lead singer of boy-band East 17 in the 1990s, who is now fit again after falling out of his Mercedes and driving over himself in 2005. Then there is Liz McClarnon, one-third of Atomic Kitten, a girl-band that “took a break” in 2004 and never returned. Big Brovaz, an R&B/hip-hop group that fell apart after one member was caught smuggling drugs and another emigrated to Australia, is back with its four remaining members. And Scooch, a foursome manufactured in 1999 and dropped by its record label in 2000, has also re-formed to compete.

All this suggests that the Eurovision is morphing from a chance for unknowns to become famous into just another venue for the interminable and lucrative soap opera that is celebrity life. It is not alone in making this transformation.

The reality TV show “Big Brother”, which starred supposedly ordinary (but actually very odd) members of the public, spawned “Celebrity Big Brother”, where the contestants were just as peculiar but better-known. “Celebrity Love Island” and “I'm a Celebrity...Get Me Out of Here!” followed.

Even in talent shows celebrities are now taking work from ordinary folk. The contestants in “Strictly Come Dancing”, “Dancing on Ice” and “Celebrity Wrestling” are already famous for, say, reading the weather or playing cricket.

The most biddable celebrities—and most convenient for band managers and celebrity magazines—are those who are well-known for minor achievements, such as dating a footballer or having breast implants. If something goes wrong with a component of a manufactured band, it is easily replaced. When one of the original members of Atomic Kitten got pregnant, the band's manager simply slotted in a new member.

Celebrities are also more predictably lucrative than nobodies, no matter how talented. An unknown Eurovision contestant might just turn out to be the next Celine Dion, but most probably won't.

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Reforming council tax

Vote loser

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Caution will trump valour

MEDDLING in the finances of local government is politically perilous. Margaret Thatcher was fatally weakened as prime minister by her insistence on introducing the reviled poll tax in 1990. But the council tax, a property-based levy that replaced the poll tax in 1993, has in turn become more and more unpopular as bills have shot up over the past decade.

Conscious of Mrs Thatcher's bloody fate, Labour ministers have played for time. First they set up an inquiry in 2003 when there was uproar about a record 13% increase in average council-tax bills. Then in July 2004 they turned to Sir Michael Lyons, a former municipal boss, to conduct another review. His final report, originally scheduled for the end of 2005, is expected close to the budget on March 21st.

The extension of Sir Michael's inquiry was prompted by a volte-face by the government 18 months ago. Council tax varies according to the value of residential properties, which are grouped into eight tax bands. Those in the top tier are charged double the standard “band D” rate and three times the bottom rate. The bands and the place of homes within them are still based on valuations made in 1991. Yet in September 2005 Labour shelved a long-overdue revaluation in England that was planned to affect bills from this April.

That cop-out now looks like smart politics. Already in a sea of troubles, Labour would be facing a tidal wave of protest in the May council elections if revaluation had gone ahead. The reason is that it produces a lot of losers even if total council-tax revenue remains the same, as ministers have pledged. Homeowners whose properties have gone up in value particularly fast in the past 15 years would find themselves in higher bands, with higher taxes.

According to an interim report from Sir Michael, a revaluation based on prices in April 2005 would push 18% of homes up one band and another 1% by two or more bands. The research also shows that the revaluation would create council-tax winners—homeowners whose properties had done less well in the housing market. In all, 17% would find themselves in lower tax bands than before.

The snag, as politicians know all too well, is that the winners from tax reform take their gains for granted whereas the losers cry foul. Other mooted reforms to council tax would add to the pain. One option, for example, would stretch the tax-band scale by adding one or more new tiers at the top, with tax rates more than three times those in the bottom tier. This would particularly upset homeowners in London and the south-east, where property values are especially high.

Despite the political sensitivity of council tax, it makes up only a quarter of local-authority funding; the rest comes from the Treasury. Reforms under Labour are unlikely to remedy this imbalance. The British state will stay extraordinarily centralised by European and American standards, says Tony Travers of the London School of Economics. Overall, ministers judge that the political benefits from reforming local-government finance are low and the costs are high. Despite its long gestation, Sir Michael's report will probably give birth to a mouse.

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Boots in play

Bitter pill

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The chemist is the healthiest it has been in years. Why change the prescription?

BRITAIN may have moved on a little since Napoleon's day, but for private-equity investors it remains a nation of shopkeepers. Five weeks after news broke of a bid for J. Sainsbury (a supermarket chain), Kohlberg Kravis Roberts (KKR), an American private-equity firm, announced a £9.7 billion offer for Alliance Boots, Britain's largest chain of chemists, on March 9th. If the deal goes through, it will be the largest of its kind so far in Europe.

Even in a country that prides itself on its open economy, nerves get a little frayed when outfits such as KKR (which was also involved in the bid for Sainsbury's) gather at the checkout tills. In the past four years Marks & Spencer, WH Smith, Debenhams and HMV have all either flirted or tussled with buy-out firms. Suspicion lingers that private-equity firms are just asset-strippers in pin-striped suits. Yet if Boots indeed vanishes from public view, critics of private equity may struggle to make that case.

Unlike Sainsbury's, which owns more than £7.5 billion-worth of land that could easily be sold and leased back, Boots already leases most of its stores. John Ralfe, in a note for RBC Capital Markets, an investment bank, thinks the owned shops that remain would fetch just £1.5 billion. And although the firm's balance sheet shows debt at a relatively light £1.1 billion, Mr Ralfe reckons its lease commitments add the equivalent of another £1.5 billion to its debt. So relying on financial engineering alone to produce big profits for new owners looks risky.

Nor, like WH Smith or Marks & Spencer when they were pursued, is Boots in especial need of new managers to give it a sharp kicking in private. That might have been useful a few years ago, after an ill-advised expansion had combined car parts and children's clothes with laser eye surgery, botox and dentistry.

But Richard Baker, its chief executive, has sold many of its esoteric operations. By sprucing up the company's tatty stores a bit, he has managed to increase its share of the market for health and beauty products, despite competition from supermarkets. And he has exploited a trusted brand to strengthen Boots's grip on filling prescriptions, a task few Britons entrust to supermarkets. The wholesale drugs-distribution business has also been expanded through a £7 billion merger with Alliance Unichem, a chain of pharmacies.

The bid, if successful, would simply recycle many of the existing top team, not least Stefano Pessina, the chemist's executive deputy chairman (and biggest shareholder), who has teamed up with KKR. People close to the talks say that Mr Pessina, who built up Alliance Unichem before pushing it into a “merger of equals” with Boots, thinks that the demands of quarterly reporting make it too hard for the firm to restructure in a way that might dampen earnings in the short term but improve long-term profitability.

He has a point. Analysts at Sanford Bernstein, for instance, raised their valuation of Boots from £8.95 a share before the bid to £10.60 after it, in part because they felt able to include estimates of future earnings that they had excluded before.

Institutional shareholders now worry that perhaps they have been too mean in assessing Boots's prospects, given that Mr Pessina thinks it such a bargain even after the 16% rise in its shares in the past year. Yet he too has cause for reflection. Part of his well-paid job was to explain its strategy to the market, and his bid is an admission that he did it poorly. If the deal goes ahead, he stands to benefit handsomely nonetheless. If it fails, Boots is likely to be looking for a new deputy chairman.

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Bagehot

Brave Dave v Cautious Gordon

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Steve O'Brien

Climate change is helping David Cameron re-brand his party. But at what risk?

David Cameron

OF THE many things that can be said about Gordon Brown few would disagree with three: he is cautious, he thinks strategically and he is not a fashion victim. For these reasons, and a few others, Mr Brown played a long game to ensure that the pound was not subsumed by the euro. Global warming presents him with a different set of political problems, but his approach will be the same. He will not want to get too far ahead of public opinion and he will be sceptical of bowing to anything that looks too much like political fashion.

It would be hard to exaggerate just how fashionable climate change has become in Britain in a short time. According to a recent poll by YouGov, 85% of the public are now convinced that global warming is actually taking place and almost as many think that without prompt action it will accelerate. Other polling companies confirm that in recent months the environment is now nearly on a par with the state of the health service, schools and immigration when it comes to what is worrying voters.

Some of the credit for this change in sensibility belongs to Tony Blair. It was the prime minister who decided to make pushing for an agreement on measures to tackle global warming one of the two planks of Britain's chairmanship of the G8 in 2005 (the other was poverty in Africa). For Mr Blair it was a perfect issue—a big international cause with a moral dimension that would require all his powers of persuasion to cajole less visionary world leaders into taking necessary action. As an added benefit, it wasn't Iraq—and for once Britain would be on the opposite side of the argument from the Americans, albeit in a polite, non-finger-pointing sort of way.

But for all Mr Blair's pioneering efforts, it is David Cameron who can claim to have done most to make climate change the topic of the moment. It is probably fair to say that without the pressure (and the cover) that has come from Mr Cameron, the government which Mr Brown will soon lead would not be committing itself to the kind of measures called for by this week's draft bill on climate change (see article).

By the time he became Tory leader 16 months ago, Mr Cameron had already identified climate change as the issue that was most capable of changing people's perceptions of his party. In the aftermath of the

2005 election, when the old tunes had been tried again and found wanting, Mr Cameron began thinking about how to break apart the Blair electoral coalition and undermine the appeal of the Liberal Democrats to well-educated, upscale voters, especially younger ones who no longer even considered voting Conservative.

For Mr Cameron the key was to attack the belief that Tories, were the “nasty party” of selfish individualists. The slogan “we're all in this together” was coined and concern for the environment was identified as the way to give it substance. At the same time, Mr Cameron could reassure party traditionalists that he was reviving an older Toryism which valued the notions of conservation and responsible stewardship. Instead of a triumphalist torch of liberty, the party adopted for its logo a washed-out-looking tree.

As a way to improve the party's image, Mr Cameron's strategy of using concern about climate change as a metaphor for the new caring, sharing Conservative Party has been a great success. The party is now getting its best poll ratings for 15 years and is being taken seriously as a future government.

But therein lies a problem for Mr Cameron and an opportunity for Mr Brown. In the past, no mainstream party has been able to outbid the Lib Dems when it came to greenery. A vote for the Lib Dems was a way of declaring one's green credentials without risking the possibility that a government might come to power and insist on inconveniently green things. Now Mr Cameron is challenging not just Labour but also the Lib Dems to bid against him in the pursuit of a low-carbon society.

The risks of such a contest for the Tories were made evident this week. Mr Cameron, to coincide with the government's draft bill and an important speech on the environment by Mr Brown to the Green Alliance, took the wraps off the latest Tory party thinking about how to curb the growth of air travel. One proposal would force frequent flyers who exceed a new “green air-miles allowance” to pay higher individual taxes to travel. The reaction in Conservative newspapers such as the *Daily Telegraph* and the *Daily Mail* was spluttering indignation, and even MPs close to Mr Cameron's circle found themselves nervously wondering what measure might next become party policy.

Scars on their backs

If Mr Cameron is scarred by people's perception of his party as nasty and selfish, Mr Brown, for his part, is scarred by the revolt against his fuel-tax escalator in 2000. It remains to this day the one serious government crisis that he has had to deal with personally. Mr Brown believes that although voters say they are keen to do the right thing on climate change, they are not yet, and may never be, ready to welcome harsh fiscal penalties to force a change in their lifestyles. David Miliband, the environment secretary, is already saying gleefully that the Tories want to “criminalise” air travel. Mr Brown prefers to offer incentives to good behaviour, for example by offering subsidies for insulating homes. The fact that people will have to pay for these carrots through their taxes will not, he hopes, occur to them.

On this, at least, Mr Cameron's economics are better than the chancellor's. His is also the moral position—no one should object to the principle of the polluter paying. But his political judgment is more open to question. Tory success has rarely been built on outbidding Labour in asking voters to accept individual sacrifice for the sake of the collective good. It is a high-stakes gamble. Cautious Gordon may well have the last laugh over Brave Dave.

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Learning about the past

Where history isn't bunk

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TASS

Across the world, approaches to teaching children about their nation's past are hotly contested—especially at times of wider debate on national identity

IF THE past is a foreign country, the version that used to be taught in Irish schools had a simple landscape. For 750 years after the first invasion by an English king, Ireland suffered oppression. Then at Easter 1916, her brave sons rose against the tyrant; their leaders were shot but their cause prevailed, and Ireland (or 26 of her 32 counties) lived happily ever after.

Awkward episodes, like the conflict between rival Irish nationalist groups in 1922-23, were airbrushed away. “The civil war was just an embarrassment, it was hardly mentioned,” says Jimmy Joyce, who went to school in Dublin in the 1950s.

These days, Irish history lessons are more sophisticated. They deal happily with facts that have no place in a plain tale of heroes and tyrants: like the fact that hundreds of thousands of Irish people, Catholic and Protestant, fought for Britain during the two world wars.

Why the change? First because in the 1980s, some people in Ireland became uneasy about the fact that a crude view of their national history was fuelling a conflict in the north of the island. Then came a fall in the influence of the Catholic church, whose authority had rested on a deft fusion between religion and patriotism. Also at work was an even broader shift: a state that was rich, confident and cosmopolitan saw less need to drum simple ideas into its youth, especially if those ideas risked encouraging violence.

As countries all over the world argue over “what to tell the children” about their collective past, many will look to Ireland rather enviously. Its seamless transition from a nationalist view of history to an open-minded one is an exception.

A history curriculum is often a telling sign of how a nation and its elites see themselves: as victims of colonialism or practitioners (either repentant or defiant) of imperial power. In the modern history of Mexico, for example, a big landmark was the introduction, 15 years ago, of text-books that were a bit less anti-American.

Many states still see history teaching, and the inculcation of foundation myths, as a strategic imperative; others see it as an exercise in teaching children to think for themselves. And the experience of several countries suggests that, whatever educators and politicians might want, there is a limit to how far history lessons can diverge in their tone from society as a whole.

Take Australia. John Howard, the conservative prime minister, has made history one of his favourite causes. At a “history summit” he held last August, educators were urged to “re-establish a structured narrative” about the nation's past. This was seen by liberal critics as a doomed bid to revive a romantic vision of white settlement in the 18th century. The romantic story has been fading since the 1980s, when a liberal, revisionist view came to dominate curricula: one that replaced “settlement” with “invasion” and that looked for the first time at the stories of aborigines and women.

How much difference have Australia's policy battles made to what children in that cosmopolitan land are taught? Under Mr Howard's 11-year government, “multicultural” and “aboriginal reconciliation”, two terms that once had currency, have faded from the policy lexicon.

But not from classrooms. Australia's curricula are controlled by the states, not from Canberra. Most states have rolled Australian history into social-studies courses, often rather muddled. But in New South Wales, the most populous state, where the subject is taught in its own right, Mr Howard's bid to promote a patriotic view of history meets strong resistance.

Judy King, head of Riverside Girls High School in Sydney, has students from more than 40 ethnic groups at her school. “It's simply not possible to present one story to them, and nor do we,” she says. “We canvass all the terms for white settlement: colonialism, invasion and genocide. Are all views valid? Yes. What's the problem with that? If the prime minister wants a single narrative instead, then speaking as someone who's taught history for 42 years he'll have an absolute fight on his hands.”

Tom Ying, head of history at Burwood Girls High School in Sydney, grew up as a Chinese child in the white Australia of the 1950s. In a school where most students are from non-English-speaking homes, he welcomes an approach that includes the dark side of European settlement. “When you have only one side of the story, immigrants, women and aborigines aren't going to have an investment in it.”

Australia is a country where a relatively gentle (by world standards) effort to reimpose a sort of national ideology looks destined to fail. Russia, by contrast, is a country where the general principle of a toughly enforced ideology, and a national foundation story, still seems natural to many people, including the country's elite.

In a telling sign of how he wants Russians to imagine their past, President Vladimir Putin has introduced a new national day—November 4th—to replace the old communist Revolution Day holiday on November 7th. What the new date recalls is the moment in 1612 when Russia, after a period of chaos, drove the Catholic Poles and Lithuanians out of Moscow. Despite the bonhomie of this week's 25-minute chat between Mr Putin and Pope Benedict XVI, the president is promoting a national day which signals “isolation and defensiveness” towards western Christendom, says Andrei Zorin, a Russian historian.

Because trends and ideas take time to trickle down from the elite to the classroom, Russian schools are still quite liberal places. In a hangover from the free-ranging tone of Boris Yeltsin's presidency, teachers can portray the past pretty much in whatever way they choose. But they are bracing for a change. As one liberal history teacher frets: “I can imagine that in a year's time we will be obliged to explain the meaning of the new holiday to first-year pupils.” And part of the meaning is that chaos—be it in the Yeltsin era or prior to 1612—is a greater evil than toughly enforced order.

In South Africa, where white rule collapsed at the same time as communism did, the authorities seem to have done a better job at forging a new national story and avoiding the trap of replacing one rigid ideology with another. “The main message of the new school curriculum is inclusion and reconciliation,” says Linda Chisholm, who helped design post-apartheid lessons. “We teach pupils to handle primary sources, like oral history and documents, instead of spoon-feeding them on textbooks,” adds Aled Jones, a history teacher at Bridge House school in Cape Province. It helps that symbols and anniversaries have been redefined with skill. December 16th used to be a day to remember white settlers clashing with the Zulus in 1838; now it is the Day of Reconciliation.

By those standards, parts of the northern hemisphere are far behind. A hard argument over history is under way in places like south-eastern Europe: this battle pits old elites that see teaching history as a strategic issue against newer ones that hope for an opening of minds.

In modern Turkey, classrooms have always been seen as a battleground for young hearts. Every day, children start the day by chanting: “I am a Turk, I am honest, I am industrious”—and woe betide the tiny tot who stumbles because Turkish is not his main tongue. Secondary schools get regular visits from army officers who try to instil “national-security awareness”.

In such a climate, it is inevitable that “history is considered a sensitive matter, to be managed by the state,” says Taner Akcam, a Turkish-born historian, whose frank views on the fate of Ottoman Armenians in 1915 have exposed him to harassment by Turkish nationalists, even in America where he now lives. But text-books have changed recently, under pressure from the European Union: the latest still call the British “sly and treacherous” but are a little kinder to the Greeks. Neyyir Berktay, an educationalist, calls the new books “significantly better” than what went before; but they are still far from accepting the idea of more than one culture within Turkey's borders.

In neighbouring Greece, there is a bitter controversy over a new textbook for 12-year-olds. Its approach is a challenge to some historical vignettes that are dear to modern Greek hearts: for example the idea of “secret schools” where priests taught youngsters to read and write in defiance of their Ottoman masters.

While Ireland's religious nationalism is in retreat (because the Catholic Church has lost influence), Greece's Orthodox leaders, like Archbishop Christodoulos of Athens, are putting up a harder fight to preserve the nationalist spirit which their predecessors embraced, reluctantly at first, in the 19th century. Ranged against them is a new school of Balkan history that reflects a cross-border dialogue between scholars. The net result is a fairer story—though when books try to be fair there's always a risk of being bland, says Thalia Dragona, a Greek educational psychologist.

Meanwhile some Greeks retort that 11 or 12 is too young to go looking for facts. In a web-discussion of the new Greek textbook, one participant thunders: “At university, the goal of historical research is the discovery of truth. But in primary schools history teaching has an entirely different aim—to form historical consciousness and social identity!”

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Israeli and Palestinian history

So hard to reconcile

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Some grown-ups want a common view, but their kids are kept apart

FEW foundation myths are as diametrically opposed as those of Jews and Palestinians. In the original Jewish narrative, the creation of the state of Israel in 1948 meant redemption, an escape from the genocidal persecution of the Nazis and a return to the land promised by God (for the religious) or historical precedent (for the secular). For the Palestinians, it was the *nakba*, the Disaster: banishment from their ancestral homes as the innocent victims of aggressive Jewish nationalism.

Time has mollified both these tales. Most Palestinians, even if they still do not think Israel's birth at their expense was justified, accept that the place now has to be allowed to exist. Most Israelis, too, have come to accept the Palestinians' own right to self-determination, and Israeli "revisionist historians" have rewritten the academic accounts of the country's birth to reflect its mistreatment of the native population. What the two sides teach their children, though, are still quite different things.

Three years ago the Israel-Palestine Centre for Research and Information (IPCRI), a think-tank in Jerusalem, conducted studies of some school textbooks on both sides. It found gradual improvements over previous years, but still a lot of problems. Israeli books sometimes contained stories that promoted pluralism and co-existence and contained positive images of Arabs. But there were also portrayals that were paternalistic and played on stereotypes and fears. Descriptions of the 1948 war tended to suggest that Palestinians either left their homes voluntarily, selling them to Jews, or were encouraged to leave by other Arabs—rather than, as sometimes happened, being forced out violently. Maps of pre-1948 Palestine sometimes underplayed the extent of Arab habitation, while maps of modern Israel never included the "Green Line", the pre-1967 border; this makes the occupied territories of Gaza and the West Bank look as if they were an integral part of Israel.

Palestinian books, similarly, had a mixed record on portraying people from the other side. IPCRI's researchers noted that they contained no calls for Israel's destruction or incitements against Judaism, but sometimes glorified "martyrdom" and the need to liberate the national homeland, while being vague about just how much of it to liberate. Their maps, too, suffered from geographical amnesia—often showing all of Palestine without Israel's borders, or displaying Arab cities in Israel but not Jewish ones.

And neither side makes much attempt to explain the other society and its history. "You learn the Israeli side of the story, where the Palestinians are present as an incomprehensible actor that sometimes upsets the apple cart," says Dov Khanin, an Israeli parliamentarian from the far-left Hadash party. Israeli textbooks also do not cover the recent history of the Oslo peace process, in which Israel began to accept the Palestinians' right to a state: a previous education minister vetoed the attempt to introduce it.

The current minister, Yuli Tamir, is pushing for improvements, says Gershon Baskin, IPCRI's co-director. She recently ordered Israeli schoolbooks to show the Green Line, and seems more serious about enforcing the mandatory teaching of Arabic, which has been allowed to lapse. On the other side, however, Hamas's election to the Palestinian Authority seems to have brought some backtracking: where the Green Line had started appearing in recent editions of a textbook for older children, in the latest issue it has disappeared again, and a mention of the "Protocols of the Elders of Zion", a notorious anti-Semitic text, was put in—only to be removed after howls of international protest.

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Positive prejudice

Really loving your neighbour

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Why holding off from hatred may not be good enough

“I FEEL comfortable when I hang out with them.” “I'm truly interested in understanding their point of view.” “I feel I can be myself when I am around them.” “To enrich my life, I would try to make more friends (from that group).”

Such warm, exuberant feelings towards other categories of human being—national, religious, racial or social—are the sort of thing that Todd L. Pittinsky, a social psychologist at Harvard University, spends his time probing and testing. This is not just because he too likes to hang around people who accentuate the positive. Mr Pittinsky's hope is to turn the conventional wisdom of “conflict studies” and “race relations” upside down.

There is a huge body of knowledge, he says, on prejudice against races or other categories. What he wants to promote, both as a scholarly tool and policy goal, is “allophilia”—liking for other groups—and the behaviour it inspires. “So much research aims to understand racist and xenophobic attitudes, so much policy aims to counter such attitudes—but people neglect to look at positive attitudes to other groups,” says Mr Pittinsky, a professor at Harvard's Centre for Public Leadership.

He believes that “allophilia” is a measurable state of mind* with hard consequences. For example, the attitude of an American voter towards immigration is determined less accurately by party affiliation or social and economic status than by the degree to which he or she simply likes Latinos. And people's choices in charitable giving, study, voluntary work and travel are guided, not surprisingly, by the sort of groups that make them feel good.

More controversially, allophilia theory holds that efforts to fight racism often err in trying to abolish or minimise the difference between groups—telling people that “we and they are really the same” or “we all belong to a bigger group, and that matters more than any slight difference.”

The experience of Bosnia and Rwanda, where murderous hatreds resurfaced after decades of apparent symbiosis, shows that categories are resilient. That is one reason why Mr Pittinsky thinks that “mere tolerance is inherently unstable.”

He is not the only scholar to stress the limits of tolerance alone as an ideal. Robert Hayden, a social anthropologist at the University of Pittsburgh, has coined the term “antagonistic tolerance” to describe the way sacred sites were shared by Christians and Muslims in the Ottoman world, and by Hindus and Muslims in British India. His point? The fact that groups accept a regime or “truce” imposed by an imperial power does not mean they will refrain from competing once they get a chance.

To ex-subjects of the Soviet imperium, talk of officially encouraged admiration for “fraternal” nations, laced with displays of embroidery, cuisine and folk-dancing, sounds cloying. Soviet allophilia finally failed because people saw it was dishonest; it hid the travails of ethnic groups who had suffered deportation and persecution under Stalin. By the end nobody believed in brotherly love.

So by all means, let allophilia be studied, measured and encouraged. Just remember: state-sponsored cultural events may not be the best way to go about it.

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* Pittinsky, T. L., Rosenthal, S. A., & Montoya, R. M. “Moving Beyond Tolerance: Allophilia Theory and Measurement”. Presented to the

Society for Personality and Social Psychology, January 2007

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Fit at 50?

Mar 15th 2007
From The Economist print edition

AFP

The European Union has been far more successful than anyone expected when the Treaty of Rome was signed half a century ago. But, argues John Peet (interviewed here), it now has three big problems to solve

ON MARCH 25th 1957 a gaggle of leaders from six European countries (France, West Germany, Italy and the Benelux trio) met in the great hall of the Horatii and the Curiatii in Rome's Capitoline museum. Behind them two 17th-century frescoes depicted ancient Rome's bloody history: a suitable backdrop, since one of their concerns was to prevent a recurrence of Europe's internecine wars. They signed a treaty to establish a European Economic Community (EEC), soon to become known as the common market. Next weekend the present crop of European Union leaders will gather in Berlin (because Germany holds the rotating EU presidency) to mark the 50th anniversary of this historic step towards European integration.

The German chancellor, Angela Merkel, wants the Berlin summit to issue a ringing declaration about the values and successes of the EU. She sees this as a way to relaunch the “European project”, which many think has been in serious trouble ever since French and Dutch voters rejected the draft EU constitution in the summer of 2005. Shortly afterwards Jean-Claude Juncker, prime minister of Luxembourg, which then held the EU's presidency, declared solemnly that “the EU is not in crisis; it is in deep crisis.” Jacques Delors, who was president of the European Commission from 1985 to 1994, says that the present “crisis” is the worst in the project's history—worse than the period of Charles de Gaulle's “empty chair” in 1965, or Margaret Thatcher's persistent demands for “our own money back” between 1979 and 1984.

Yet today's difficulties should not be allowed to obscure Europe's achievements of the past 50 years. True federalists actually saw the Treaty of Rome as a move away from the building of a European superstate that they had hoped would develop from the European Coal and Steel Community, set up in 1951. But in fact the EEC grew out of two other events: the French National Assembly's rejection of the proposed European Defence Community in 1954 and the Suez crisis of 1956. The first pointed to a reassertion of nation-states at the heart of Europe; the second led France to conclude that a European community was in its vital interest.

A bigger objection to the EEC was that it covered only a small part of Europe. Soviet-dominated eastern Europe was excluded, as were fascist Spain and Portugal, because they were not democracies. But Britain and others chose to stand aside, either because they disliked the political integration implicit in the new grouping or because they wanted to preserve their neutrality. Indeed, two years after the Treaty of Rome came into force, seven countries (Austria, Britain, Denmark, Norway, Portugal, Sweden and

Switzerland) set up the rival European Free-Trade Association (EFTA). “Seven and Six” was how this newspaper greeted the news (see article).

Fifty years later the European Economic Community has changed out of all recognition, having metamorphosed into the European Union and grown far beyond the original six members. Despite the EFTA experiment, Britain applied for membership only four years after the Treaty of Rome, but was blocked by de Gaulle's veto and did not join until 1973, along with Denmark and Ireland.

Several waves of further expansion followed, including Spain and Portugal in 1986. The biggest of all saw the admission of ten new members, including many ex-communist central European countries, on May 1st 2004. At the start of this year Romania and Bulgaria became the EU's 26th and 27th members. Plenty of others are clamouring to be let in. The only countries that have chosen to stay out even though they would instantly qualify for membership are Iceland, Norway and Switzerland.

The European Union has also moved far beyond the economic sphere. The completion of the single market was set in train only in the 1980s and remains a work in progress. But just as the American government used the constitution's interstate commerce clause to expand its powers, so the European institutions have exploited single-market rules to extend their responsibilities into such areas as social policy, welfare and the environment. Along the way the EU has acquired a single currency, a common foreign policy, a passport-free travel zone and policies on justice and home affairs, plus a nascent defence alliance with its own military-planning staff.

This does not sound like an organisation in deep crisis. Even in the past two years the EU has agreed on a seven-year budget and set out ambitious plans for an energy policy and for tackling climate change. It has sent troops as far afield as Aceh and Congo and co-ordinated big national deployments in Lebanon. It has started membership negotiations with Croatia and, most momentously, with Turkey. Claims that this club has been unable to function since 2005 seem overblown.

The 50-year itch

Yet the EU does face three huge, related problems. The first is what to do about its draft constitution, which was signed in October 2004 in the very room that witnessed the signing of the Treaty of Rome. The constitution's declared purpose was to improve the functioning of the institutions, to clarify the distribution of powers and to bring the union closer to its citizens. But because it was turned down in the French and Dutch referendums, the treaty has not been ratified.

Ms Merkel hopes that the Berlin declaration will not only relaunch the EU but also start resuscitating the constitution. Yet the task she has taken on is immense. Any new treaty must not only be unanimously agreed on but also ratified by all of the union's 27 members before it can take effect.

That seems much less likely to happen because of the second big problem facing the union: popular disenchantment with the project. As Mr Delors notes, there is no dream, no vision that strikes a chord with today's European citizens in the way that reconciliation and an end to war did 50 years ago. Most of today's leaders, he complains, devote their time to attacking Brussels and all its works, not to spreading the word about the EU's achievements.

The mistrust of the union is perhaps most pronounced in Britain, but the regular opinion polls taken by Eurobarometer reveal high dissatisfaction with the union in other countries as well. In many of them, voters seem strongly opposed to further enlargement. The French and Dutch “no” to the constitution reflected this bleak mood. The new members are more enthusiastic about the union than the old ones, but even in them it is not hard to discover Eurosceptics.

This special report will weigh the chances of making progress with the EU constitution or devising some other “institutional settlement”, to use the current catchphrase in Brussels. It will consider how this is affecting plans to admit yet more new members. And it will assess the debate over how to persuade Europe's citizens to take a less jaundiced view of their union. But it will start by considering the union's third and perhaps most serious problem: the poor performance of its economies in recent years.

It was the roaring economic growth of the EEC, above all else, that made it such a success in its early days. It was this economic dynamism, too, that lured first Britain and then all the others to apply for membership. Conversely, it was gloom about the economy, and particularly over persistent high unemployment, that played the biggest part in the rejection of the constitution and in the spread of

Euroscepticism across the continent. If the EU is to flourish far beyond its 50th birthday, it is its economy that most needs attention.

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Are you sitting comfortably?

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A brief refresher course on the workings of the European Union

THE nuts and bolts of the European Union are hardly riveting, but a basic knowledge of its institutions is essential to understanding how it works, so here is a quick reminder.

At the heart of the EU, as envisaged by its French founding father, Jean Monnet, is the **European Commission**, to which each national government appoints one commissioner for a five-year term. The "college" of 27 commissioners sits atop a 20,000-strong bureaucracy that constitutes the EU's executive. The commission also has the sole right of initiating legislation, administers the budget and has other independent powers including deciding competition cases and representing the union in trade negotiations.

The commission takes its political cue from the **European Council**, made up of the 27 heads of government, which meets four times a year and also nominates the commission president. The European Council is, in practice, the highest incarnation of the **Council of Ministers**, the main law- and budget-making body, which brings together national ministers (eg, of finance, foreign affairs or agriculture). The presidency of the council rotates every six months, so each country now gets to be in the chair once every 13½ years. The council often makes decisions by qualified majority, a weighted system of national votes, but on some issues (eg, taxation) it has to be unanimous.

As part of the council, the **high representative** for foreign policy reports to national governments and may (or may not) work closely with the commissioner for external affairs. The common foreign and security policy he runs is not part of the classic Monnet machinery (sometimes known as the "community method"), but is formulated by the member governments. The same is true for most policies on justice and home affairs.

The other law- and budget-making body is the **European Parliament**. It has 785 members, directly elected in rough proportion to each country's population. Like the commission, the parliament serves for five years; unlike the commission, which is in Brussels, it holds its plenary meetings mostly in Strasbourg, though committees meet in Brussels. Most EU laws are subject to "co-decision" by the council and parliament, but in some areas, including justice and home affairs, the parliament has no say. The parliament has to approve the choice of commission president and can dismiss the entire commission, but not individual commissioners.

The **European Court of Justice**, based in Luxembourg, acts as the EU's supreme court in areas for which the union is responsible (which does not include criminal law, for example). There is one judge per country. A court of first instance helps with the caseload. Cases are decided by simple majority. Luxembourg also hosts the Court of Auditors, which checks EU spending—and qualifies the accounts every year.

The EU has a plethora of other agencies, as well as the Luxembourg-based European Investment Bank, the world's biggest multilateral borrower. Among the more puzzling are two Brussels-based advisory bodies: the Economic and Social Committee, which brings together the "social partners", and the eponymous Committee of the Regions. Between them they cost some €150m ($200m) a year to run, and nobody can remember what they are for. But this being the EU, nobody dares to scrap them either.

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The quest for prosperity

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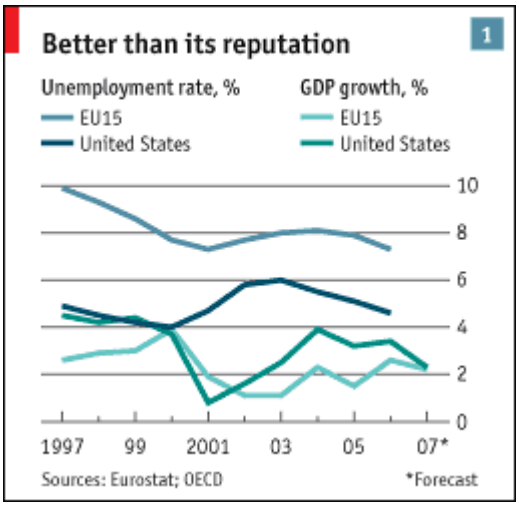
Europe's economy has been underperforming. But whose fault is that?

AS IT happens, the recent economic figures in Europe have been better than anyone dared hope. The German economy, in the doldrums for six long years, is at last gathering speed. In 2006 GDP in the EU as a whole grew by 2.9%, and in the euro area by 2.7%. In the fourth quarter of last year the euro area's GDP growth outstripped America's for the first time in five years. Average unemployment has fallen to 7.5%, the euro area has generated 12m new jobs over the past eight years and even productivity growth has started to pick up. Across Europe the mood has become noticeably more optimistic.

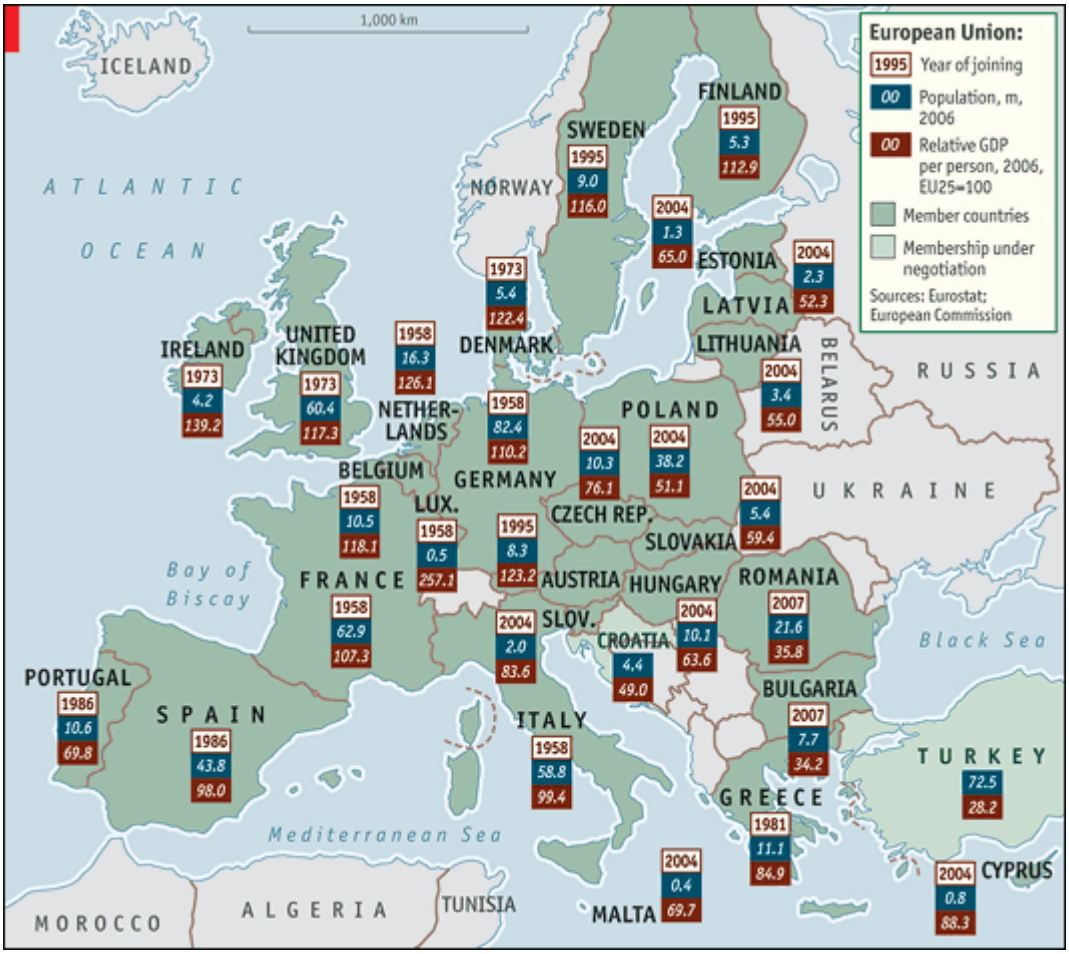
Yet this greater optimism comes after an extended period of profound gloom. Over the past decade GDP growth has been generally lacklustre; productivity has stagnated, in some countries even fallen; and unemployment has stayed stubbornly high (see chart 1). The contrast with 50 years ago, when the Treaty of Rome was signed, could hardly be greater. West Germany was in the midst of its *Wirtschaftswunder*, a miracle country of rapid growth, low unemployment and fast-rising living standards. France was enjoying *les trentes glorieuses*, 30 splendid post-war years when everything went right. And Italy was quickly gaining ground on its richer European neighbours.

Some slowdown after the catch-up years of the 1950s and 1960s was inevitable. Reconstruction after the war had boosted growth; the movement of workers out of farming and into industry had raised both productivity and GDP; and many more women had entered the labour force, lifting output. Once these effects had run their course, rapid growth became much harder to sustain.



The same factors played a part in other rich countries, such as America. Yet the EU economies, and especially the euro area, have in recent years performed much less well than the American economy, which is comparable in size. GDP per head in the euro area is almost 30% lower than in America, and the gap is widening: the OECD reckons that trend growth per person is only about 1.5% a year, compared with America's 2%. Productivity growth in Europe slowed in the late 1990s, whereas in America it speeded up. Unemployment in Europe has been persistently higher than across the Atlantic. Europeans have also been slower to take up information technology, and the economic climate has been less conducive to innovation and research and development (R&D).

The transatlantic gap can be exaggerated: much of America's faster GDP growth merely reflects faster population growth and longer hours of work, and differences in measurement also play a role. But the perception that over the past decade Europe has stopped catching up with America, and in some respects actually fallen behind, is broadly accurate.



Europe's response has come in two main forms: the creation of the euro in 1999 and the drawing up of the so-called Lisbon Agenda in 2000 to boost the EU's competitiveness. The Lisbon Agenda set an ambitious goal for Europe: to turn it into “the most competitive and dynamic knowledge-based economy in the world” by 2010. The plan was to promote liberalising reforms, increase R&D spending and encourage the deregulation of labour and product markets across the continent. Similarly, the euro's proponents hoped that the single currency would not only increase cross-border trade but also, by imposing tougher price and wage discipline on its members, speed up structural reforms in all European economies.

Yet even the most fervent EU enthusiast would concede that these hopes have come to little. Joaquín Almunia, the economics commissioner, maintains that the current revival is linked to the structural reforms made in recent years, which may be starting to pay off. But most economists put it down to two other factors: a cyclical upswing and a huge improvement in German competitiveness after years of real wage restraint. If they are right, it is reasonable to doubt that today's recovery will prove sustainable—and to fear that Europe's economies could slip back into their previous underperformance.

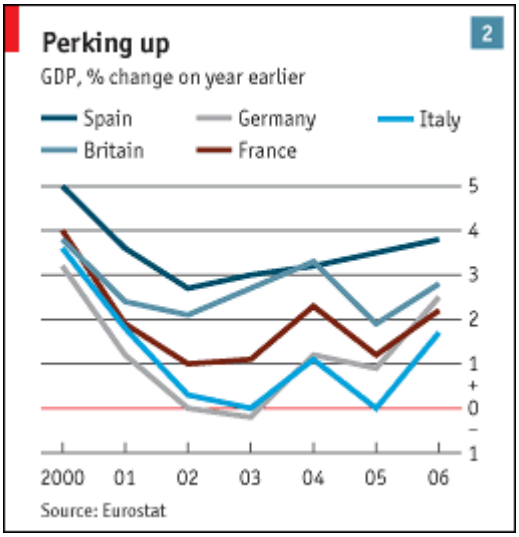
Look on your doorstep

So what is Europe's problem? First, whatever it is, it is not Europe-wide, nor indeed linked to the euro. This supposedly sclerotic continent includes three of the world's five best-performing and most competitive economies: Denmark, Finland and Sweden. Britain and Ireland have also done well in recent years. Nor is it only north European economies that have put in a spurt: Spain, too, has grown fast since 1999. Of these six success stories, three are in the euro zone and three are not.

The poor performers in Europe have been the core countries of the euro, in particular France, Germany and Italy (see chart 2). Since these three account for two-thirds of euro-area GDP, their failings have led to slow growth for both the euro area and the EU as a whole. It is evident that Europe's economies have sickened at national not European level, so it is at national level that the cures are needed.

Nor is there much disagreement among economists about what those cures should be. In all three countries labour and product markets are too highly regulated, holding back employment

growth and making their economies less flexible. Both the IMF and the OECD have been urging further liberalisation as the only sure route to better economic performance. Even Europe's political leaders understand this, though they are also swift to spot political obstacles to reform. As Luxembourg's Mr Juncker once said, “we all know what to do, we just don't know how to get re-elected after we've done it.”



Mr Almunia hopes that the recent improvement in the EU economies may break the unfortunate cycle of partial reforms that take time to bear fruit and are often followed by election defeats. But there is another, less hopeful possibility: that opponents of change will treat the present recovery as a sign that no further reforms are needed.

Within the euro area a debate is in progress over whether the single currency itself encourages or discourages reforms. Most of its progenitors had hoped for the first. The euro has clearly boosted intra-EU trade, by somewhere between 5% and 15%, according to the OECD. It has also been a spectacular success from a technical point of view, establishing itself not just as a viable currency but as the only plausible rival to the dollar. For example, it now accounts for 25% of global foreign-currency reserves. Yet the euro's broader economic impact has been limited because of its members' failure to liberalise enough. As the OECD puts it in its most recent report on the region, “insufficient flexibility prevents the euro area reaping the full benefits of economic and monetary union.”

When the euro began, critical economists directed most of their fire at the stability and growth pact, which attempted to set rigid limits on budget deficits run by euro members and threatened huge fines if those limits were breached. This provision made little economic sense. Because the single currency deprived members of monetary and exchange-rate flexibility, they were likely to need more, not less, fiscal flexibility. Predictably enough the stability pact was swiftly bust by France and Germany, after which it was fitted with extra loopholes.

Since then the pact has become much more accommodating as more and more countries have breached the budget-deficit ceiling of 3% of GDP. Mr Almunia maintains that it is now sufficiently flexible to set a reasonable long-term path for those euro-area members that still need more fiscal consolidation. In particular, the level of public debt remains too high in Italy, Belgium and Greece, and to a lesser extent in France and Germany (see chart 3).

But the failure of the euro countries to liberalise has become a much more pressing concern. Not only is it holding back the euro area as a whole, it is also increasing the divergence between members. This shows up most clearly when comparing movements in unit labour costs.

The coming crunch

Germany initially suffered from entering the euro at a high exchange rate, but over the past seven years German companies have spectacularly improved their competitiveness, thanks mainly to keeping a tight rein on wages. This is at the root of Germany's economic recovery and has allowed it to claim back from America its position as the world's biggest exporter. But part of this improvement has come at the expense of other euro members with which it is now locked into the single currency. In particular, the Mediterranean quartet of Italy, Spain, Portugal and Greece has suffered a huge loss of competitiveness in a relatively short time (see chart 4).

This loss is reflected in colossal current-account deficits (eg, 8.5% of GDP for Spain, which has been growing fast) or pitifully slow growth (only 1.3% a year for Italy since the euro began). Without the euro, Italy at least would surely have had to devalue by now. In a sense, the single currency has protected its members, but at

the price of storing up big problems in future. Some analysts still speculate that Italy might one day be forced out of the euro.

That would be politically unthinkable, and most politicians in Rome duly refuse to think about it. Leaving the euro would also be costly, as Argentina found when it was forced off its currency peg to the dollar in 2001. So what else can Italy do? One possibility is to follow the German example and endure years of wage restraint. But that requires a lot of discipline. Moreover, the two-tier labour markets that have become common in Europe, with insiders on permanent contracts insulated from the fears of unemployment afflicting temporary workers, offer little incentive for workers to accept real pay cuts.

The harsh conclusion is that, for euro members, there is no alternative to substantial reform, liberalising product and labour markets alike, to make their economies more flexible and better able to cope with shocks. Ironically, the two EU members with arguably the most flexible economies are Britain and Denmark, both of which have chosen not to join the euro. Alas, the political leaders in Mediterranean countries show little appetite for taking on the special-interest groups that always resist painful reforms.

Meanwhile the new EU members that were once pressing for early entry need to think again. Slovenia scraped in at the start of this year; Malta and Cyprus may follow soon. But the Baltic states do not seem ready; and Poland, Hungary and the Czech Republic, the three biggest new members, are unlikely to join before 2012 at the earliest. They would be wise to employ the waiting time not only to grow fast but also to make their economies more flexible.

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Constitutional conundrum

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Damned if they do and damned if they don't

IT IS clear that economic reform ought to be at the top of the EU's agenda, especially for euro members. Yet Germany, currently in the EU president's chair, is mostly ignoring it. That may be because the German economy is looking good at the moment, or because Ms Merkel's grand coalition of Christian and Social Democrats cannot agree on further reforms. But it is also because she has lit on another priority altogether: to revive the EU constitution rejected by French and Dutch voters.

The story of the constitution (or more accurately, constitutional treaty) is tedious, but it must be told to explain why the EU is in turmoil. In truth, too much of the past 20 years has been spent debating the union's institutions, a process usually triggered by an inter-governmental conference (IGC). The trouble is that each IGC (and consequent treaty) has left some national governments dissatisfied, leading to perpetual calls for yet another IGC and treaty (see table 5).

A treaty too far? 5
EU treaties

	Year signed	Year in force	Main provisions
Single European Act	1986	1987	Majority voting, single-market legislation by end-1992
Treaty on European Union (Maastricht)	1992	1993	Monetary union, common foreign policy, justice and home affairs; Danish opt-outs added later
Treaty of Amsterdam	1997	1999	Social policy, more majority voting, incorporation of Schengen passport-free zone
Treaty of Nice	2001	2003	New voting system, smaller commission, provisions for enlargement to 27; Irish declarations added later
Constitutional Treaty	2004	Not ratified	More majority voting, new institutional settlement, establishes a constitution for Europe

Source: *The Economist*

This game began with the Single European Act in 1986, which extended qualified-majority voting to a whole raft of policy areas because that seemed the only way to push through the legislation needed for the 1992 single-market programme. Jacques Delors, then the commission's president, seeded the act with references to monetary union, and three years later another IGC was summoned against British wishes (an IGC can be called by simple majority, even though any new treaty needs unanimous agreement). That produced the Maastricht treaty of 1992, which not only promised to create a single currency by 1999 but also set up a common foreign and security policy and new arrangements for co-operating on justice and home affairs.

Maastricht was followed by Amsterdam and then Nice, agreed on after a nightmare four-day summit chaired by France's president, Jacques Chirac, in December 2000. That made three new treaties in the space of eight years, none of them wholly satisfactory. In 2001 an EU summit at Laeken, outside Brussels, considered what were termed the Nice leftovers: simplification, greater transparency, a bigger role for national parliaments and subsidiarity (the buzzword for ensuring that decisions are taken at the lowest sensible level of government). But rather than call yet another IGC, the Laeken summit decided to summon a convention in which representatives of the EU institutions, national governments, parliaments and the public could debate what to do.

Time for a little constitutional, says Merkel to Barroso

The convention on the future of Europe was chaired by a patrician former president of France, Valéry Giscard d'Estaing. Eager to leave his mark, Mr Giscard d'Estaing soon persuaded his colleagues to go well beyond their Laeken remit and, in a deliberate invocation of America's Philadelphia convention of 1787, draft a full-blown constitution for the EU. The result was not, however, an elegant 20-page document like its model, but a 300-page behemoth which was presented to another EU summit in mid-2003.

The first part of the new text features institutional changes. These include a new council voting system that reflects countries' populations; an extension of qualified-majority voting and of co-decision-making with the European Parliament to most legislation; a permanent president of the council, in place of the six-monthly rotating presidency; a new foreign minister, to combine the jobs of high representative and external-affairs commissioner; and a smaller commission. It also provides an exit clause for any members who might wish to leave the club.

Part two of the constitution consists of a charter of fundamental rights, first drawn up as a declaratory statement at Nice. A lengthy third part comprises a consolidated and slightly amended version of all previous treaties.

There followed another IGC, featuring more rows about institutions, but in mid-2004 a text of the constitutional treaty was unanimously agreed on. The snag was that by then as many as 12 governments had promised to put the constitution to a referendum at home before ratifying it—including Britain, France, the Netherlands, Spain and Poland, as well as ballot-happy Denmark and Ireland.

The campaigning for these referendums was mostly shambolic. Mr Chirac sent copies of the entire, largely incomprehensible, text to all French voters. The Dutch government refused to campaign at all. With so many national governments mired in unpopularity and economic troubles, it was scarcely surprising that opinion polls in both countries started to turn against the treaty, even after Spanish voters had said yes in February 2005. On May 29th French voters rejected it by 55% to 45%, and on June 1st Dutch voters turned it down by 62% to 38%.

This was not the first time that countries had said no to Europe. Norway twice voted against joining the club at all. The Danes rejected the Maastricht treaty in 1992 and the Irish the Nice treaty in 2001. After both these rejections a few adjustments were made, some declarations added and the verdicts reversed in a second vote. The Danes and Swedes also voted against joining the single currency.

Yet the French and Dutch snub to the constitution in 2005 still came as a huge shock: it was the first time that two countries had said no simultaneously, the first time any big country had done so, and the first time a founder member had rejected anything. When a few weeks later an EU summit failed to agree on a budget for 2007-13, the sense of crisis was complete.

Picking up the pieces

Since the double rejection the EU has officially been observing a “pause for reflection”. The trouble is that even now, nobody knows what to do. The French and Dutch governments have made it plain that they are not prepared to follow previous practice and submit an only slightly revised text to a fresh vote. Others, notably the British, Poles and Czechs, now balk at ratification as well. But 18 of the 27 EU

countries have endorsed the constitution, and no fewer than 20 recently met in Madrid to declare themselves its “friends”. Germany is especially keen to stick to most of the present text, if only because the new voting system in the council would substantially increase its weight.

Ms Merkel plans to present the June EU summit with a “road map” for taking the constitution forward. Each country has nominated two officials to meet in secret to prepare this—a bizarre decision, since one purpose of the constitution was to increase transparency. The timing is very tight, because a new French president will be chosen only on May 6th, and the new French National Assembly will not be elected until June 17th, four days before the summit. There will also loom the prospect of a new British prime minister, presumably Gordon Brown, preparing to take over from Tony Blair.

Yet whatever the political permutations in different countries, it is clear that there are only four broad options:

•**Treaty plus**. This would add material to the present text, such as more social protection (an EU-wide minimum wage?), plus perhaps new provisions on such currently fashionable topics as energy and the environment. The word “constitution” might be quietly dropped. The Spanish and other governments favour something along these lines, as apparently does the Socialist presidential candidate in France, Ségolène Royal. But the British government is not alone in strongly opposing more social measures. And such a maximalist document would surely have to be put to the vote again in several countries, including the two that said no in 2005, risking another rejection. Ms Royal has said she would like to hold a fresh referendum on an expanded treaty in 2009.

•**Treaty minus, with a promise of more to come.** This option was first branded by Nicolas Sarkozy, the main centre-right candidate in France, as a “mini-treaty”, though he has since dropped the term. It would adopt only the big institutional changes in the constitution—a new voting system, the foreign minister, a permanent president of the council and more majority voting (but drop the smaller commission). Such a text might be called an amending treaty, which could be ratified by national parliaments alone, in time for the 2009 European election. Yet cherry-picking from the present document would upset the delicate compromises that went into it. The Irish and perhaps the Danes might still have to vote, which could lead to demands for referendums elsewhere. To reassure maximalists, the rest of the constitution might be put off to a further convention or IGC to be summoned soon after 2009, but others would not find that prospect reassuring at all.

•**Treaty minus, with a promise of no more to come**. This is a slimline version of Mr Sarkozy's mini-treaty, favoured notably by the British, who do not want to hold a referendum or be dragooned into another huge convention or IGC. It would adopt the sort of small treaty proposed by Mr Sarkozy, but probably with no extension of qualified-majority voting. It would be purely a piece of institutional tidying-up, which could be ratified by national parliaments on the promise that nothing else would soon be put before them. Even so the Irish would have to vote, as might the Danes if the new treaty transfers any new powers to Brussels. And any such document would cause deep dissatisfaction in most of the 18 countries that have already ratified the full constitution.

•**Nothing at all**. This is the option if all else fails. It also sometimes seems to be the preferred choice of Britain, and perhaps of Poland, the Czech Republic and even the Netherlands. All four countries have reservations about some of the institutional provisions in the present text, even if they are wrapped up in a mini-treaty. For example, the British are against the charter of fundamental rights and most extensions of qualified-majority voting; the Poles oppose the new voting system; and the Dutch dislike the proposed foreign minister. But the do-nothing option will satisfy neither those who argue that the EU of 27 cannot continue as it is, nor those who have already ratified the constitution. It is also awkward because the Nice treaty specifies that the commission to be chosen in 2009 must have fewer commissioners than member countries, and its voting provisions extend only to Romania and Bulgaria. The absence of any new treaty could thus become a big obstacle to further enlargement (see article).

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Over the next few months negotiators will concentrate on these four options, or variants of them. Two concerns will be uppermost in their minds. The most important will be that the union cannot afford another failed ratification. In several countries that points to avoiding a referendum at almost any price. This desire could put the countries seen to be most at risk of losing such a vote (Britain, France, the Netherlands and perhaps Poland) in a strong bargaining position should a new IGC be convened—except that these four do not agree on what they want.

The second concern will be to achieve something, anything. José Manuel Barroso, the commission president, is a pragmatist who has spent the two years since the French rejection urging that the EU should concentrate on what it can deliver best—in fields as diverse as foreign policy and energy security. But he complains that, wherever he goes, half the questions he is asked are about the constitution. The feeling of unfinished business haunts everything else that the EU does, which is why so many countries are anxious to avoid the do-nothing option.

New members will come CAP in hand

Budget blues

Into this combustible mix is about to drop another issue that has been largely neglected recently: the EU budget. The financing package for 2007-13 agreed on in December 2005 included a clause promising a thorough budgetary review in 2008. This was a concession to the British, who had to give up a chunk of their budget rebate to get a deal. Mr Blair had demanded further reform of the common agricultural policy (CAP) as his price for negotiating on the rebate, but Mr Chirac's intransigence blocked that. The promise of a review became a face-saving device for Mr Blair.

Now, however, the budget review is acquiring new significance, for three reasons. The first is that the commission is taking it seriously. The EU budget, at just over €115 billion, or 1% of the union's GDP, is relatively small. But it is also ludicrously archaic. Mr Blair rightly pointed to the absurdity of devoting almost half of all EU spending to the CAP (though that is an improvement on the 1980s, when the CAP absorbed 70%). A further one-third of the budget goes on regional support, especially for infrastructure spending, but nearly half of that regional money is bagged by relatively rich countries. Only a tiny fraction of the budget is spent on projects that might further the Lisbon Agenda's goal of promoting high-tech growth.

These blemishes were pointed out forcefully in the 2003 Sapir report, written at the commission's own request. The report recommended cutting CAP spending to nothing and redirecting regional spending to poor countries, with the balance of the budget being either returned to national governments or devoted to such worthier activities as R&D. But when the commission and the council drew up the budget for 2007-13, they largely ignored these recommendations. Still, Sapir sets a useful framework for the budget review.

The worst feature of the EU budget is that, to make up for spending so much on the CAP when some member countries have so few farmers, it is littered with rebates. The British rebate, bludgeoned out of her partners by Margaret Thatcher's handbag-wielding in 1979-84, is the best-known, but the Germans, Dutch, Austrians and Swedes now all have special rebates of their own. Indeed, the latest budget row in Brussels is over how far countries that get rebates should contribute to others' rebates. A useful aim for the budget review would be to put paid to this Alice-in-Wonderland world altogether.

The best way of doing that would be to tackle the CAP once and for all. In fact it has already changed far more than its critics allow. Since 2003 most farm subsidies have been switched to direct payments, not linked to production and therefore not trade-distorting (whereas American farm subsidies have shifted the other way). A growing chunk of the money goes on rural-development projects, not farming as such. Feeding into the budget review is a mid-term “health check” of the CAP to be conducted by the agriculture commissioner, Mariann Fischer-Boel. She wants to cap payments to individuals, shift even more spending to rural development and scrap milk-production quotas.

An idea she is not keen on is national financing of the CAP. When farm subsidies took the form of price support, they had to be paid at EU level because products crossed borders. But as they switch to direct payments, the case for financing at EU level is weaker: there is no reason why national governments should not pay for their own farmers. Several countries favour partial national financing of the CAP, as does the budget commissioner, Dalia Grybauskaite. More surprisingly, so do some influential Frenchmen, including Alain Lamassoure, an MEP who is one of Mr Sarkozy's advisers. The French realise that, when

the full panoply of farm support extends to central Europe (it is now being phased in), they will become net contributors to the CAP. Indeed, opponents of future farm reform will be found not in Paris but in Warsaw and Bucharest.

Looking for a bargain

The time is thus ripe for another attack on the CAP and the way it is financed. And that adds another reason for paying attention to the budget review: that it could become linked to the fate of the constitution. The timing is tricky, because negotiations on the constitution could start later this year and the budget review is not starting until next year. And the odds of a quick deal on the constitution remain low. Britain, the main architect of the budget review, is a big obstacle to a renewed treaty. And it is no secret that Mr Brown, as chancellor of the exchequer, strongly opposed the EU budget deal in December 2005.

Yet there are now whispers in Brussels about one of those grand bargains often struck at EU summits: give Mr Brown a serious dose of CAP reform, including some national financing, and he might accept a revised constitution after all. Certainly it makes sense that a new treaty should be accompanied by a fresh look at the budget. Other countries might buy the idea if they see a prospect of getting not only a chunk of the constitution (perhaps with an understanding that more might come later) but also an end to the hated British rebate, which would become redundant if CAP reform were sufficiently bold.

Any such bargain would, however, take time and patience to strike. With a new French president and a new British prime minister, it will certainly be hard to do before 2009. Meanwhile another issue may come to a head: further enlargement of the union to the western Balkans, starting with Croatia. The trouble is that several countries, as well as the commission itself, have said that there cannot be any further enlargement without an institutional settlement. Thus enlargement, a key foreign-policy goal for the EU, has also become hostage to the constitution.

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The ins and outs

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The EU's most effective foreign-policy instrument has been enlargement. But how far can it go?

IT IS sometimes said that the European Union is an economic giant but a political pygmy, with no foreign policy to speak of. Certainly foreign and defence policies, above all others, remain largely in the hands of national governments; and foreign-policymaking with 27 countries, every one of them with a veto, is inherently difficult. Last year, for example, Poland alone blocked the start of negotiations on a new partnership agreement with Russia. Yet to conclude that the EU has no foreign policy at all would be wrong.

Getty Images

A vote against further enlargement too

For a start the union is the world's biggest aid donor, which gives it great sway in Africa, parts of Asia and the Middle East. It has also acquired military heft, with troops deployed (sometimes with NATO, with which links have not always been close enough) in Bosnia, Congo, Darfur and Kosovo. Chris Patten, a former external-affairs commissioner, suggests that success in Afghanistan is now crucial to the EU's credibility, as well as NATO's. In the diplomatic world the union also pulls more weight. Javier Solana, the high representative for foreign policy, is in touch with the American and Russian foreign ministers at least as much as his British, French and German counterparts.

Consider Iran and nuclear proliferation. Besides having their hands full with Iraq, the Americans have no diplomatic relations with the government in Tehran. So Britain, France and Germany were entrusted with trying to persuade the Iranians not to build a nuclear weapon. Mr Solana soon joined the trio on behalf of the wider EU. Their approach may not have been particularly successful, though it has probably strung the process out—but it has been a substantial example of a common EU foreign policy in the making.

If any version of the EU constitution were ever adopted, it would bolster the common foreign policy by turning the high representative into a “foreign minister”. More important than the exact title of this person would be three accompanying changes: merging the job with that of the external-affairs commissioner, giving it extra clout and money; setting up a common EU external service that could, in time, become more important than national diplomatic services; and making the foreign minister the permanent chairman of EU foreign ministers' meetings.

Yet even this would not resolve the biggest weakness in the EU's foreign policy: that it cannot work when national governments disagree with each other. This was most obvious over Iraq, on which the EU as a whole did next to nothing. It has also often been true of relations with Russia. The new east European EU members generally take a tougher line than older members; and the Russians, as Europe's chief

suppliers of energy, have proved adept at playing divide and rule. Even on China, internal differences have persisted over whether to end the EU's arms embargo. No institutional change can alter these, even though polls suggest that a common approach to foreign policy is near the top of the list of what voters want from the EU.

By far the most successful EU foreign policy has been its own expansion. In the 1980s the prospect of joining played a critical part in ensuring a smooth transition from dictatorship to democracy in Greece, Spain and Portugal. More recently it has transformed the east European countries as they moved from communist central planning to liberal democracy. The countries of the western Balkans have been pacified and stabilised after the bloody 1990s thanks mainly to their hopes of EU membership. And Turkey has made wholesale changes in its politics, economics and society largely to boost its chances of joining. Indeed, judged in terms of success in exporting its values to its backyard, the EU has done much better with its neighbours than the United States has with central and south America, largely because of the carrot of enlargement.

After this year's arrival of Romania and Bulgaria, there is further work to do in south-eastern Europe. Entry negotiations began with Croatia and Turkey in October 2005, and are due to start with Macedonia some time in the next 12 months. EU foreign ministers also acknowledge that the only way to prevent the Balkan tinderbox of Serbia, a newly independent Montenegro and a would-be independent Kosovo from exploding again is to hold out to the whole region the prospect of joining their club. Yet the very notion of further enlargement is now in question, for three reasons.

Enlargement fatigue

The first and perhaps most serious is a decline in support for enlargement among EU voters. Opinion polls for the whole union still show a narrow majority in favour, but in some countries the mood has turned sharply against. The French and Dutch rejections of the constitution in 2005 partly reflected dissatisfaction over the 2004 enlargement. Olli Rehn, the enlargement commissioner, complains that EU governments have made little effort to spell out the beneficial effects of that enlargement to their voters, even though a commission analysis shows that the economies of new and old members alike have done well out of it—with the three countries that fully opened their labour markets to workers from the new entrants immediately, Britain, Ireland and Sweden, gaining the most.

The second, related reason is that, partly in response to the new arrivals in 2004, many EU governments have lost enthusiasm for enlargement. This is particularly true of France, Germany and Austria. Although Mr Chirac has always favoured Turkish accession, he did not speak in favour of it when it became an issue in the referendum campaign in 2005. Instead, he amended the French constitution so that a referendum is now required on all future new entrants after Croatia. Germany's Angela Merkel is no fan of enlargement and has long argued against Turkey's entry (though her government is willing to let the negotiations proceed for now). Austria is even more hostile to Turkey, though it would like to take in the countries of the western Balkans in its own backyard.

The third reason, inevitably, is the failure to ratify the constitutional treaty. In part this is because of an age-old argument known, in the EU jargon, as widening v deepening. Brussels folklore has it that widening (admitting new members) naturally conflicts with deepening (further integration of existing members). To avoid this, expansion has often been timed to coincide with treaty changes: a key motive for the treaties of Maastricht, Amsterdam and Nice was the knowledge that the east Europeans were waiting in the wings. This time round, the constitution was meant to provide the deepening: if it is blocked, that raises questions over further widening.

Some critics also see the lack of an institutional settlement as a bar to enlargement, arguing that the EU's machinery, initially designed for six members, cannot function effectively with 30 or more. The Nice treaty provided votes and parliamentary seats for Romania and Bulgaria, but not for Croatia (though in practice the necessary changes, along with a new deal on the size of the commission, could go into Croatia's accession treaty, which like all treaties must be ratified by all EU members). This argument is aimed mainly at Britain, which opposes attempts to revive the constitution but is the chief proponent of more enlargement. The none-too-subtle message is that turning down the first would mean losing the second.

A Turkish tangle

The elephant in the room in all discussions about EU enlargement is Turkey, which was one of the earliest applicants to the European club and was accepted as eligible back in 1963. The Turks were miffed to be overtaken by the east Europeans in the 1990s (one Turkish general wondered whether his country would have done better to spend 40 years in the Warsaw Pact instead of NATO). The EU, for its part, argued that Turkey was far from fulfilling the “Copenhagen criteria” for membership (which include democracy, a free-market economy, observance of human and minority rights, and political stability).

When the mildly Islamist Justice and Development Party won the Turkish election in 2002, it soon proved itself a bigger reformer than the fiercely secular governments that preceded it. Recep Tayyip Erdogan, who became prime minister in March 2003, made it his top priority to get Turkey ready to join the European Union. Over the next two years his government passed a huge array of constitutional and judicial reforms to that end. He won his reward in October 2005, when the EU opened membership negotiations with Turkey.

Unfortunately things have mostly gone downhill since then. After making such efforts to qualify, the Erdogan government lost its reforming zeal. Relations with the Kurds in Turkey's south-east, which improved when the government scrapped many of its most repressive laws, deteriorated again after the Kurds of northern Iraq cemented their autonomy and the separatist PKK guerrillas resumed fighting following a ceasefire. Moreover, the Turks soon ran into predictable trouble over Cyprus.

Eyevine

Will Europe open its doors?

A condition for the opening of membership talks was that Turkey extend its customs union to all the 2004 entrants, which included Cyprus. Admitting the (Greek-Cypriot) republic without settling its dispute with the (Turkish-Cypriot) north was, as Lord Patten concedes, “a mistake”. A UN plan to reunite the disputed island fell apart in April 2004 when the Greek-Cypriots, who had been promised membership of the EU in any event, overwhelmingly rejected it in a referendum. (The Turkish-Cypriots, desperate to be admitted to the EU as well, endorsed it.)

An exasperated EU promised to alleviate the isolation of the Turkish-Cypriots, but as full members the Greek-Cypriots now have a veto over this. In December 2006 the Turks refused to open their ports and airports to the Greek-Cypriots because nothing had been done for the north—so the EU suspended negotiations on eight of the 35 “chapters” in the membership talks.

Heading off a train-wreck

Mr Rehn insists that this is not a “train-wreck”, noting that good technical progress is being made and a new chapter will be opened shortly. He describes the commission's approach as firm but fair. There is a case for a breathing-space in EU-Turkish relations ahead of Turkey's presidential and parliamentary elections later this year. He suggests that the right course is to muddle through the rest of 2007. Croatia may join the club “about the turn of the decade”. After that the Turks will have a choice: to resume their reforms, putting their talks back on track towards membership later in the decade, or to turn away from the road towards Europe altogether.

The trouble is that the issue may come to a crunch sooner than that. Mr Sarkozy and his advisers are explicitly saying that Turkey has no place in the EU. Many Germans note with horror that, if Turkey ever joins, it is likely on present demographic trends to become the most populous member by 2020, with more voting weight and more MEPs than Germany. Elmar Brok, a German Christian Democratic MEP who until this year chaired the European Parliament's foreign-affairs committee, says it was wrong to open negotiations in the first place, and the more honest course would have been to tell the Turks that they must settle for something short of full membership. Yet Turkey refuses to contemplate anything second-class.

A fallout between the EU and Turkey, one of its biggest and most important neighbours, would be disastrous. It would surely put an end to any hopes of settling the Cyprus problem. Worst of all, many Muslims would see a failure of Turkey's membership hopes as a rebuff administered by a Christian club. Not only would that further sour the West's relations with the Islamic world; it would also cause disaffection among the EU's own 15m-strong Muslim population, many of whom are already hostile to the

countries they live in.

A close eye is being kept on Turkey and the western Balkans by those with membership aspirations of their own: Ukraine, Moldova, Belarus, and countries in the Caucasus and even north Africa. The union has not so far recognised any of these as actual or even potential candidates for membership. Instead it has adopted a “neighbourhood policy” that is supposed to cover such bread-and-butter issues as aid, trade concessions and immigration and visa policies.

Living with the neighbours

Yet the neighbourhood policy suffers from an inherent structural flaw. It is meant to apply equally and without discrimination to countries that may one day join the EU, and to countries that will never do so. However, the first group will always have an entirely different agenda: to them any neighbourhood policy is a mere stopgap until they can begin the long march towards membership. Countries that can never hope for this might be readier to invest in making the neighbourhood policy itself more substantial.

So is it time to define the boundaries of the EU? Even enthusiasts for enlargement think it may be approaching its natural limits. The western Balkans, now surrounded by EU countries, obviously ought to be in. Moldova, Ukraine and Belarus also seem likely candidates. There might be more doubt over the Caucasus, which is even farther off—though Georgia makes no secret of its ambition to join. But north Africa would be off most lists of potential candidates. Morocco has been told that it is ineligible because it is not part of Europe. Talk of the Roman empire, of the Mediterranean as *mare nostrum* or of Algeria's and Morocco's old status as parts of France and Spain will change few minds.

To say now where enlargement will end might also be a good way to reassure nervous voters in existing member countries who have turned against the idea. But their nervousness reflects mainly a failure on the part of EU leaders to explain the benefits of expanding the club, not a hostility to any specific countries (Turkey being perhaps an exception). And it would seem odd to set limits now to a policy that has worked such wonders. If Turkey and Cyprus, why not—one day—Lebanon? Why not Israel (already a participant in the Eurovision song contest)? Indeed, why not—another day—Morocco or Russia, both of which have a strong European heritage and culture?

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Four Ds for Europe

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Dealing with the dreaded democratic deficit

THE biggest failing of the EU has long been the yawning gulf between the union, as both a project of integration and a set of institutions, and the mass of its citizens. Nobody could pretend that, when French and Dutch voters voted against the constitution in 2005, they were objecting merely to specific provisions in the text; nor that they were just using the opportunity to give their governments a good kicking. It seems much more likely that they were expressing a general feeling of resentment towards the European project and its remoteness. That feeling is more emphatic in some countries than in others, but it seems to be strong everywhere.

EPA

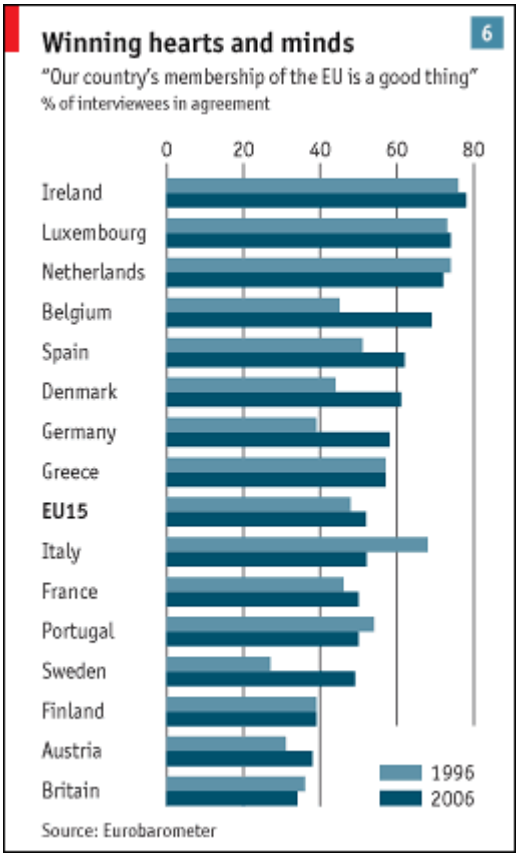
An expensive and unloved talking-shop

The traditional response by governments has been to ignore such resentment. Europe was always an elite project, went the argument, and so it should remain. As long as political leaders understood and pursued the case for European integration, that should be enough. French voters would probably have refused to endorse the creation of the European Coal and Steel Community back in 1951, and German ones, if given a voice, might have vetoed the abolition of the D-mark in favour of the euro 50 years later.

But ignoring the people's views is no longer tenable. Margot Wallstrom, a commission vice-president, even deplores the word “club” as connoting an elitist institution. Politicians these days have to be more responsive to voters. Mindful of this, many leaders in Europe spend more time attacking the Brussels institutions for interference (even though almost all EU laws require those leaders' endorsement) than preaching the European dream. The media have also become more critical of the EU. And the spread of referendums means that the people in the member states must now be repeatedly persuaded of the case for Europe. In the past 15 years a dozen national referendums have been held on EU questions (not counting acceding countries)—and half of them have been lost.

Popular support for the EU has, in fact, risen a bit in most countries over the past decade (see chart 6), but it remains dismayingly low. Worries over this lay behind the Laeken declaration, the convention on the future of Europe and the ill-fated constitutional treaty. But whatever the ultimate fate of the constitution, it is not going to be a vehicle for regaining voters' affection. That leaves three other options.

Love me do



The first is to concentrate on showing European citizens that the union works. Mr Barroso, the commission's president, is keen on this idea. In the economic field, it means persisting with the Lisbon Agenda for further reform and liberalisation across Europe. To this can now be added the related issues of energy and the environment, as examples of areas where it is self-evident that EU governments should be co-operating (though what is really needed is global co-operation). Foreign policy is another area where most European citizens believe that a union acting together can do more than nation-states acting alone.

A concentration on delivery does not always mean doing more at European level. Indeed, the arguments on subsidiarity over the past decade suggest that there is merit in giving back to nation-states some of the powers that Brussels has arrogated to itself over time. Mr Barroso's commission has repeatedly promised to review and scrap some of the torrent of regulations and directives that has poured out of Brussels in the past 20 years, and it also claims to subject new regulatory proposals to a more rigorous cost-benefit analysis than before. There has been more talk than action, but at least the amount of new legislation being proposed by the commission has dramatically declined over the past decade.

The second idea for making the EU more popular with its citizens is to deal with what is known as its democratic deficit. Eurosceptics make much of the European institutions' lack of transparency and accountability, their corruption and their remoteness from the citizens. They note that the commission is not merely far away from most national capitals but unelected (although the last thing a Eurosceptic wants is an elected commission), and yet perhaps 80% of the laws passed at national level originate in Brussels.

This is a seductive line of reasoning, but it is flawed. There is indeed a democratic deficit in Europe, but it is hard to maintain that it lies at the European level. In comparison with most national governments the Brussels machinery is highly transparent: information is always easy to find. Corruption certainly exists, as it does everywhere; but the auditors' habitual qualification of the EU's annual budget relates largely to how the money is spent at national level. As for accountability, the commission answers not only to national governments, through the council, but to the parliament as well.

In truth, the deficit is to be found more at national than at European level. The EU is a creature unlike any other: neither a superstate, nor a federal union, nor an inter-governmental organisation. But it is closer to the third, in that nation-states remain the main actors. Against this background the failure of democracy has been not to make clear to citizens that they can find out about and influence what is going on in Brussels through national institutions. Yet this ought to be easy, since the senior law-making body, the Council of Ministers, is made up of national governments.

As it happens, there is an example of how this might work: Denmark. When the country joined the then EEC in 1973, the Danish Folketing (parliament) was anxious not to lose its ability to steer legislation, despite the loss of sovereignty to Brussels. So it set up a powerful European committee to call ministers to account. This committee summons ministers every Friday to discuss the following week's council meetings in Brussels, and agrees to a negotiating mandate. If ministers want to deviate from this mandate, they must telephone from Brussels to secure fresh instructions from the committee, which can reconvene at a moment's notice.

It sounds cumbersome, but it seems to work—and it certainly gives Danes a greater sense of understanding of and involvement in the EU. The EU committee in the Folketing also maintains a large information and library service and a website that all Danish citizens can use. Denmark's famously Eurosceptic voters have become noticeably more relaxed about their country's EU membership over the past decade, even as hostility to Brussels has grown in some other countries.

A distant parliament

What about the European Parliament? It has a reputation as an expensive talking-shop, with a ludicrous monthly commute between Brussels and Strasbourg that adds some €250m a year to its costs. But it is better than its reputation: the average quality of its members has risen, and it has learnt how to work the EU system. In the past year alone the parliament has played a crucial role in forging the necessary compromises to secure an agreement on the EU's services directive and also on REACH, a set of rules governing the use and disposal of chemicals. Its influence over the commission has increased too: in 1999 the parliament even engineered the commission's resignation.

Yet there is one area in which the parliament has failed utterly, and that is to establish its legitimacy as the natural conduit connecting citizens to the European project. Few European voters have the slightest idea who their MEP is, and fewer still know what he or she does all day. Turnout in European elections is mostly low and falling; campaigns are fought on national not European issues, reflecting in part the fact that the media are national not European; there is no sign of a Europe-wide *demos*. Voters see little connection between how they cast their ballot and what happens in the EU. MEPs form broad political groups—the centre-right European People's Party, the Socialists, the Liberals and so on—but tend to act together, not in opposition to each other. The agenda of the place, it often seems, is largely to advance its own powers.

One answer sometimes put forward to remedy this is to increase the parliament's powers. Give it more say in the choice of commission president, for example, and more voters might take an interest. In 2004 MEPs made clear to EU governments that their choice of commission president should reflect the political make-up in Strasbourg. It would be easy to entrench this practice, perhaps getting political groups to propose their own candidates if they gained a majority. Yet even if this were done, it is hard to see the parliament winning greater legitimacy.

A more robust solution would be to acknowledge that the parliament has failed in this goal and to scrap it altogether. In its place there could be a European Senate, made up of nominated members of the European committees of national parliaments (the American Senate was nominated, not elected, until 1914; the original European Parliament was nominated from national parliaments before direct elections in 1979). Such an innovation might encourage other parliaments to follow the Folketing example and improve their scrutiny of what goes on in the EU. Sadly, the union, like most international organisations, never abolishes anything.

The third idea for re-firing European citizens' enthusiasm for the club is to give them a new dream, what some have called a narrative. The original narrative for the project was about peace and prosperity. But the first is now taken for granted, except perhaps in the Balkans; and many voters feel that the EU is either not helping or is actively hindering the second. So what might a new narrative for the 21st century consist of?

Dream and reality

Concern for the environment might furnish something. A second idea would be a more active foreign policy, which might even include a renewed push for enlargement. Poles and Lithuanians are not the only people who would be pleased if Ukraine were to join the club one day: the orange revolution of December 2004 resonated all round Europe. But what is needed most is more inspired leadership by European heads of government, including a full acknowledgment to their voters of the practical importance of the EU. And in the end surely what voters really want above all is economic success and greater prosperity—which is why further economic reforms are so pressing.

Yet harder-headed Europeans may not be interested in dreams or narratives at all. As Germany's Helmut Schmidt once put it, “if you have visions, you should see a doctor.” Such folk might prefer a different reassurance: that the EU will be a group of diversity not uniformity, and that not everybody on the European voyage needs to go at the same speed. The Brussels jargon for this idea changes and evolves: recent examples include flexibility, variable geometry and a multi-speed EU. What it means in practice is that some countries opt for projects of closer integration that others prefer to avoid.

In fact this is already happening. All members must participate in the single market, with its four freedoms of movement (of goods, services, labour and capital). Most of them are also members of NATO, but some are not; only 13 of the present 27 are in the euro; a different but overlapping 12 are in the Schengen passport-free travel zone, with the addition of three non-members; and just seven have signed the Prüm treaty governing the exchange of information among police forces (see table 7). The Amsterdam and Nice treaties both provide for “reinforced co-operation”, another piece of EU jargon

referring to projects that only some countries choose to join.

Once again Denmark offers an interesting case study. The Danes are almost as famous for their supposed Euroscepticism as the British. When they voted no to the Maastricht treaty in 1992, it was renegotiated to give the country four opt-outs: from the single currency (from which Britain was also excused, but Sweden was not, so although it has chosen to stay out of the euro, technically it has no right to do so); from defence policy; from EU citizenship; and from justice and home affairs.

Living with these opt-outs can be awkward. In defence, for example, Danish forces are able to join NATO operations but must pull out if the EU takes over. And although the country retains the krone, the Danish National Bank is not independent of the European Central Bank in its interest-rate policy because it has chosen to hold the krone in lockstep with the euro. The governor, Nils Bernstein, admits that he moves interest rates two hours after the ECB does so. In the money market Denmark pays an average interest-rate premium over the euro of 0.15-0.25%, according to Mr Bernstein, which could be said to represent the cost of remaining outside the single currency. The other cost is a certain loss of influence, but a Denmark inside the euro would hardly hold huge sway.

Yet despite, or perhaps because of, their opt-outs, the Danes seem increasingly comfortable inside the EU. They no longer fear that a superstate is being built in Brussels. There is little pressure to follow the lead of Greenland, a Danish territory that holds the distinction of being the only place to have withdrawn from the club (in 1985). Nor do Danes cast envious eyes at Norway and Switzerland, the two biggest European countries to have chosen to stand aside from the union. Both must apply almost all EU laws to gain full access to the single market, and even make large payments into the EU's budget—but play no part in its decision-making.

Overlapping circles 7

Countries in...

	EU	€	NATO	Schengen	Prüm
Belgium	✓	✓	✓	✓	✓
France	✓	✓	✓	✓	✓
Germany	✓	✓	✓	✓	✓
Luxembourg	✓	✓	✓	✓	✓
Netherlands	✓	✓	✓	✓	✓
Spain	✓	✓	✓	✓	✓
Greece	✓	✓	✓	✓	–
Italy	✓	✓	✓	✓	–
Portugal	✓	✓	✓	✓	–
Austria	✓	✓	–	✓	✓
Slovenia	✓	✓	✓	–	–
Denmark	✓	–	✓	✓	–
Finland	✓	✓	–	✓	–
Ireland	✓	✓	–	–	–
Britain	✓	–	✓	–	–
Bulgaria	✓	–	✓	–	–
Czech Rep.	✓	–	✓	–	–
Estonia	✓	–	✓	–	–
Hungary	✓	–	✓	–	–
Latvia	✓	–	✓	–	–
Lithuania	✓	–	✓	–	–
Poland	✓	–	✓	–	–
Romania	✓	–	✓	–	–
Slovakia	✓	–	✓	–	–
Sweden	✓	–	–	✓	–
Iceland	–	–	✓	✓	–
Norway	–	–	✓	✓	–
Cyprus	✓	–	–	–	–
Malta	✓	–	–	–	–
Turkey	–	–	✓	–	–
Switzerland	–	–	–	✓*	–

*Approved but not yet enacted

Sources: European Commission; NATO

A multi-speed Europe could, in principle, be a way of solving several different problems at once. For example, the argument over the constitutional treaty has shown yet again that some EU members want more integration than others do. As things stand, this can lead to blazing rows, with those that want to hang back eventually being pushed into a corner from which they either veto a project or, reluctantly, sign up to it to avoid being isolated. A far better approach would be for those who have no interest in joining to allow others to go ahead—which is how the British dealt with the European single currency at Maastricht.

Equally, a multi-speed Europe might be a good way of resolving growing tensions within the union over further enlargement. Already new, often poor members are invited on the basis that they do not take part in all EU activities right from the start; they are usually given long transition periods before benefiting in full from the union's four freedoms. A multi-speed Europe might take that idea a stage further. Turkey, say, might join on the basis not just of a long transition period but of an open-ended exclusion from the EU's rules on the free movement of labour.

The risks of multi-speeding

A multi-speed Europe clearly harbours potential dangers. The EU can work only if all its members sign up to the bulk of its rules, known as the *acquis communautaire*, especially for the single market. It will not be possible for members to opt out of competition rules, for example. Indeed, most single-market laws are not suitable for the multi-speed treatment, though the single currency clearly is.

If a multi-speed Europe were to become a multi-tier Europe and those in the lower tiers felt frozen out, that would be unsatisfactory too. Most proposals to create a “hard core”, a group of “pioneers” or even a

“United States of Europe”, embracing either the original six or, more likely, the 13 euro members, fall into this category. Nor could a multi-speed arrangement work if those who pursue a project can capriciously stop others joining if they want to.

Yet it should be possible to find ways round these problems, using the European Commission and, if need be, the European Court of Justice as arbiters. The goal should be not to create categories of first- and second-class membership, nor to fragment the union. Rather it should be to accommodate diverse views on how far and how fast to go, and to take in a wider range of members—but all within a broad common framework set by the single market and the EU institutions.

In 2005, after the French and Dutch rejections, the commission published a paper by Mrs Wallstrom called plan D, outlining various ways of bringing the EU closer to its citizens. A better name for what Europe really needs might be plan 4D, to stand for democracy, delivery, dreams and diversity.

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The European Union at 100

Mar 15th 2007
From The Economist print edition

Is the best yet to come?

LIKE anybody nearing a 50th birthday, the European Union needs a makeover. But as this special report has suggested, the past two years' talk of a deep crisis is overblown. The union is functioning as well (or as badly) as it did before French and Dutch voters rejected the constitution.

The efforts by the Germans to use their stint in the EU president's chair to resuscitate the constitution may thus be as mistaken as the fatuous logo they have chosen (above). It is possible that an agreement may be reached on a minimalist treaty, but it depends on a string of heroic assumptions: that Mr Sarkozy wins the French presidency; that the Poles can be bullied into accepting institutional change; that some way can be found to buy off Britain; and that almost everybody can avoid referendums. Since at least one of these assumptions is likely to prove wrong, the odds of a successful deal on the constitution seem low.

Rather than harping on institutional reform that may never happen, the EU should concentrate on things it can achieve. That means putting forward sound policies in fields such as the environment; continuing the union's enlargement to take in the western Balkans and, ultimately, Turkey; and doing more work, both in Brussels and in national capitals, to engage citizens in the project. Above all, it means taking advantage of the present recovery to push through economic reforms.

The future of the EU is hard to predict. Over the next decade or so it could undergo a burst of further integration; it could fall apart into opposing camps of those who would go forward and those who would go back; or, perhaps most likely, it could just muddle through. So how might it look in 50 years' time?

A centenary celebration, 2057

The EU is celebrating its 100th birthday with quiet satisfaction. Predictions when it turned 50 that it was doomed to irrelevance in a world dominated by America, China and India proved wide of the mark. A turning-point was the bursting of America's housing bubble and the collapse of the dollar early in the presidency of Barack Obama in 2010. But even more crucial were Germany's and France's efforts later in that decade, under Angela Merkel and Nicolas Sarkozy respectively, to push through economic reforms.

These reforms produced a sharp fall in unemployment just as Europe began to enjoy a productivity spurt from the spread of information technology. The eventual result was a growing labour shortage, which was not resolved until the arrival of Turkey and Ukraine as full members in 2025. The accession soon afterwards of the first north African country, Morocco, helped to prolong Europe's boom.

Of course it was not all plain sailing. The great Italian crisis of 2015, when the government of Gianfranco Fini quit the single currency just as David Miliband's Britain was about to join, cast a long shadow. Yet although Italian bondholders took a hit from the subsequent default and Italy's economy was soon overtaken by Spain's, financial markets proved forgiving, and the government of Walter Veltroni managed to rejoin the euro fairly quickly. Since then no country has been tempted to repeat Italy's painful experiment.

The other cause for quiet satisfaction has been the EU's foreign policy. In the dangerous second decade of the century, when Vladimir Putin returned for a third term as Russian president and stood poised to invade Ukraine, it was the EU that pushed the Obama administration to threaten massive nuclear retaliation. The Ukraine crisis became a triumph for the EU foreign minister, Carl Bildt, prompting the decision to go for a further big round of enlargement. It was ironic that, less than a decade later, Russia itself lodged its first formal application for membership.

At the same time politicians in Brussels and Washington, grappling with the blocked Middle East peace process, had a eureka moment. EU membership had worked, eventually, in Cyprus, which was reunified in 2024; why not try it again? So it was that Israel and Palestine became the EU's 49th and 50th members.

The big challenge now is what to do about Russia. Its application has been pending for 15 years. Some say that it is too big, too poor and not European enough to join. But now that the tsar has been symbolically restored, Russia has an impeccably democratic government. A previous tsar saved Europe from Napoleon nearly 250 years ago. It would be apt to mark the anniversary by welcoming Russia back into the European fold.

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The film industry

Hollywood's new model

Mar 15th 2007 | LOS ANGELES
From The Economist print edition

AP

How new money is changing the film industry

JUDGING by the number of times each was gushingly thanked by this year's Oscar winners, the people who finance films are now more important than God. Investors are certainly omnipresent in Tinseltown these days. If all goes according to plan, they will soon resurrect United Artists, a defunct studio, and the career of Tom Cruise, a star with a public-image problem. It is just one sign among many of how money from outside Hollywood is changing the film industry.

Film has traditionally been a good business and a bad investment. The dream machine has been oiled by sources as varied as property developers, tax-averse Germans and (in the case of the 1959 film “Plan 9 from Outer Space”) the Baptist church. But returns have usually been disappointing. The inherent riskiness of the film business is one reason; another is the studios' accounting practices, which, until recently, were as laden with special effects as the films they produced.

The need for serious money has changed all that. The big studios now spend an average of just over $100m making and selling each film. Led by Disney, they are cutting back on the number of movies they produce, making the gambles they do take all the more risky. The studios' corporate parents would prefer it if their financial reports were a little less suspenseful. Hence the new, more open and honest attitude to private investors.

For the past few years the big studios have encouraged hedge funds and other investors to back “slates” of several dozen films spread over more than a year. Although the financiers are not allowed to get their hands on reliable money-makers such as “Harry Potter” or “Spider-Man”, they still find the slates less risky, and hence more appealing, than individual films. Last September Merrill Lynch estimated that outsiders cover more than 30% of the cost of film production.

One result is that Wall Street now knows much more about how the film business works. As their experience grows, some investors are beginning to think they can “beat the house”, as John Burke, a Hollywood dealmaker, puts it. Rather than backing every film put out by a studio, they are investing in producers with good records. Michael London, who specialises in making family dramas, and Joel Silver, who is notably good at blowing things up, are among the recent recipients of such largesse. Several more such deals are rumoured and the pace may increase if JPMorgan goes ahead with its plan to set up a film-finance arm.

This has changed the arc of Hollywood careers. Not so long ago, producers and film stars who fell out with studio bosses might retire to write books with titles like “You'll Never Eat Lunch in This Town Again”.

These days they round up some private equity and get back to work. Thanks to Goldman Sachs, Bob and Harvey Weinstein were able to set up a new film studio just two months after they angrily left Disney in 2005.

Tom Cruise and Paula Wagner, his producer, were talking to investors even before Paramount Pictures cut them loose last year. MGM, the largest stake in which is held by Providence Equity Partners, quickly gave them offices. It is trying to raise $500m or so to pay for the production of four to six films a year. If the deal comes off, United Artists, a moribund label owned by MGM, will return to its silent-film era roots as a studio run by the talent.

Although the big names get most of the attention, Wall Street money is churning the independent film business, too. Until recently, investors were nervous about dealing with firms that produce only a few films a year. But financiers have noticed that cheap hits such as “Little Miss Sunshine” can be hugely profitable. And beneath their maverick exteriors, such outfits are reassuringly obsessed with cost control. Jim Stern, a former fund manager who has raised enough money to start producing films, reckons he can undercut the big studios by making them for $20m-35m.

Such a minnow tries to protect its investors by pre-selling films abroad and exploiting tax rebates offered by other states to filmmakers who shoot outside California. Overture Films, a four-month-old studio, plans to follow a similar strategy. It will eschew broad teenage fare (which is expensive to advertise) in favour of movies targeted at narrower audiences such as blacks and young women.

Chris McGurk, who runs Overture, reckons that three-quarters of the newly financed outfits will be gone within five years, and he may be right. The film industry's real problem, says John Sloss, a consultant, is not so much a shortage of films as a shortage of eyeballs. Getting movies to the screen and the DVD racks, and persuading people to see them, is the tricky part. Here the established studios have a huge advantage. They have global networks and legions of marketing men—and can attach their trailers to blockbusters.

The other problem is that film is such an unpredictable business. Who could have predicted, for example, that Americans would spend some $70m in just three days last week to see “300”, a poorly reviewed film featuring a Scottish-accented Spartan warrior? Perhaps nobody—but a studio like Warner, which produced the film, probably had a better chance than a hedge-fund manager trying to beat the odds. New money is transforming Hollywood, but institutional memory will always count for something.

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Viacom and YouTube

War is declared

Mar 15th 2007 | SAN FRANCISCO
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Why both sides need a deal in the fight between old and new media

ACCORDING to Viacom, an “old-media” giant, YouTube is not only a hugely popular video-sharing website, but also a scrounger that “has built a lucrative business out of exploiting the devotion of fans to others' creative works in order to enrich itself and its corporate parent Google.” With these words, Viacom announced this week that it was suing Google and YouTube for copyright infringement and demanding $1 billion in damages. Google, a “new-media” giant and the leading web-search engine, responded that “YouTube is great for users and offers real opportunities to rights holders: the opportunity to interact with users; to promote their content to a young and growing audience; and to tap into the online advertising market.”

War has thus been declared, just as analysts and lawyers predicted five months ago when Google bought YouTube for $1.65 billion. The legal situation is ambiguous. At issue is America's Digital Millennium Copyright Act, which became law in 1998, when Google, founded that year, was unknown and YouTube did not exist. It includes a “safe-harbour” provision for anybody who removes copyrighted content as soon as the owner requests it.

YouTube has been doing that—most notably a month ago, when Viacom demanded that 100,000 clips be taken down. But the safe-harbour clause applies only as long as a site does not gain financially from infringement. Moreover, Viacom complains, YouTube uses the clause as a fig leaf, since the copyrighted clips that are taken down reappear within minutes, as other users upload them. Viacom thus needs a full-time team to police YouTube. It says 160,000 of its clips have been illegally viewed 1.5 billion times on the site.

Google's response is a subtly effective dig at Viacom's own failings. Why are Viacom's clips so popular on YouTube? Because Viacom does not make them easily available on its own sites and thus, says Google, is missing a chance to connect with users, promote its content and generate advertising revenue. Because Viacom is a dinosaur, in other words.

But YouTube also looks bad. Ostensibly it owes its stunning rise to the popularity of “user-generated content”—home videos that amateurs upload for fun. There are indeed plenty of those on YouTube. But advertisers seem unable to make any use of clips featuring dogs on skateboards or teenagers trading expletives. So YouTube's paltry revenues—about $15m last year, according to Robert Peck at Bear Stearns, a broker—in fact depend on old-fashioned, professionally produced content. This is why Google and YouTube have recently struck deals with such media companies as CBS and the BBC. Others, such as NBC and Viacom, have been holding out.

For YouTube's parent, Google, the suit, even if expected, is a headache. It is already facing lawsuits against its project to digitise books, without the explicit consent of publishers, so that relevant passages can be included in web-search results; and against its display of copyrighted news articles on Google News, where it suffered a defeat in a Belgian court last month. Now the fight extends to video.

Google may choose to take some of these suits to trial in order to clarify a principle. For instance, it can reasonably argue that its book-scanning project in effect creates a better card catalogue that helps publishers and authors. But with video clips, the suit looks like a Viacom tactic to get better terms in a deal that both sides need. This war, to paraphrase Clausewitz, is merely the continuation of negotiations by other means.

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Corporate scandals

Black clouds

Mar 15th 2007 | NEW YORK
From The Economist print edition

Policing misbehaving bosses is proving to be a costly business

TRIALS of the century have become an annual event in the business world, thanks to America's wave of corporate scandals. But the trial of Conrad Black, which began in Chicago on March 14th, may actually merit that title, at least judged as spectacle. On show will be an epic cast, led by his Lordship, a former media baron accused (with three other executives) of looting his company, Hollinger, which once owned Britain's *Daily Telegraph* and the *Chicago Sun-Times*.

Witnesses are expected to include Henry Kissinger; Donald Trump; Barbara Amiel, Lord Black's wife; and his former business partner, David Radler, who will testify against him. The $42,870 of Hollinger's cash splashed on Lady Black's birthday party is one of the main examples of the assets allegedly looted thanks to Lord Black's dominance over his company (see article). The prosecution will be overseen by Patrick Fitzgerald, fresh from his successful pursuit of obstruction charges against Lewis “Scooter” Libby. Last year *People* magazine called Mr Fitzgerald one of America's most eligible bachelors.

If Lord Black is convicted, he could face up to 95 years in jail. His lawyer, Edward “Fast Eddie” Greenspan, is likely to argue that most of the expenditures described as looting were approved by Hollinger's board, the members of which now claim to have been misled. Ominously, Dennis Kozlowski, Tyco's former boss, also said his board had approved his lavish spending. He is now serving up to 25 years in jail.

Lord Black's defenders argue that the cure has been worse for Hollinger's shareholders than the disease—though prosecutors would no doubt retort that breaking the law deserves punishment regardless. Sorting things out after his departure cost a fortune: the $200m cost of investigations far exceeds the sum taken in the alleged “corporate kleptocracy”.

The mutterings about disproportionate punishment are even louder in options backdating, the other corporate scandal of the moment. Over 140 firms have been embroiled and 70 executives have lost their jobs. Firms granting share options to employees stand accused of picking dates with particularly favourable prices. The latest twist is that some firms may have backdated options to take advantage of the plunge in share prices after the terrorist attacks of September 11th 2001, seemingly exploiting a national crisis.

Although there may be nothing illegal about backdating *per se*, failure to disclose it or properly account for it may constitute fraud. UnitedHealth Group, one of the first big firms embroiled in the scandal, last week restated its profits down by $1.55 billion over a 12-year period as a result. Last year the scandal claimed the job of its boss, William McGuire. There is speculation that Steve Jobs of Apple will be the prosecutors' next high-profile target. The board has cleared him of any wrongdoing, but admits some backdating did take place. A prosecution could prove hugely costly to Apple's shareholders, the main victims of any backdating.

The Securities and Exchange Commission is struggling to find the punishment to fit the crime. Commissioners have been deadlocked for months over whether to ratify a proposed $7m settlement with Brocade Communications, which is supposed to be the template for other fines. California's prosecutors seem to have discovered a sense of proportion, however. On March 14th all charges were dropped against Patricia Dunn, the former chairman of Hewlett-Packard, over her role in the boardroom spying scandal that shook the computer firm last year. The serious charges against three other defendants were also dropped, after they agreed to plead guilty to minor misdemeanours and do community service. So at least one trial of the century has been avoided.

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German corruption

The hollow men

Mar 15th 2007 | DARMSTADT
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Revelations at Siemens highlight what was once a culture of bribery

THE trial of two former Siemens managers, which began in Darmstadt on March 13th, is likely to be followed by more spectacular trials in Munich and Nuremberg brought by prosecutors investigating the sprawling engineering conglomerate for alleged corruption. The two former managers are accused of using at least €6m ($8m) of funds stashed in Switzerland and Liechtenstein to smooth the path of power-equipment contracts with Enel, an Italian utility. Both admit the offence. The senior man says he did not inform his superiors.

The Munich investigation is potentially more embarrassing for Siemens because it involves more money—at least €400m allegedly misappropriated in its telecoms division for bribery and other uses—and allegations against former board members. Are these isolated cases, or was there a company-wide policy of using bribes to win contracts?

Before 1999, when OECD countries outlawed the bribery of foreign officials, paying such sweeteners was widely accepted. But under German law it was still legal until August 2002 to bribe foreign-company employees, though not foreign officials. By its own admission, Siemens has had trouble weaning staff from their old ways. Winning big contracts is difficult even today without using consultants and go-betweens who expect money. “Other companies have done it more skilfully,” said one of the Darmstadt defendants privately.

The task for Siemens is to continue with business as usual elsewhere. A telecoms-equipment joint venture with Nokia was briefly postponed but is due to go ahead in April. In Brussels Osram, Siemens' light-bulb subsidiary, is fighting to maintain punitive duties on cheap low-energy light bulbs made in China. Osram, one of the world's biggest bulbmakers, says it wants to ensure “fair” competition. But as part of a group that appears to have been buying advantage for itself, that plea rings a little hollow.

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Carrefour

Crossroads

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France's answer to Wal-Mart faces some of the same difficulties

IF FIRMS are supposed to learn from their rivals' mistakes, then America's Wal-Mart and France's Carrefour are doing a bad job. Over the past few years the world's two biggest retailers have made surprisingly similar errors. Both expanded too quickly abroad. Both dithered over their focus on low prices. Both toyed with discounters and with smaller versions of their giant shops. Now both are in trouble.

Wal-Mart's troubles are mainly strategic, but Carrefour is also struggling with uncertainty over its management and ownership. On March 7th the Halleys, the family in control of Carrefour, replaced Luc Vandevelde, its chairman, with Robert Halley, a septuagenarian member of the clan. On the same day Colony Capital, a property-investment company, and Groupe Arnault, the holding company of Bernard Arnault, a French luxury tycoon, bought almost one-tenth of Carrefour.

Reuters

Carrefour attracts a buyer

The exit of Mr Vandevelde, a former boss of Marks & Spencer, a British retailer, came after weeks of speculation about Carrefour's future. In mid-February the Halleys said Bernard Bontoux, another family member, would take over from Mr Vandevelde as their representative on the board. Two weeks later the French press reported rumours of the imminent departure of José Luis Duran, Carrefour's chief executive, and Eric Reiss, its financial chief.

Then came the surprise swoop by the Arnault group and Colony. “Mr Arnault is likely to do a Vincent Bolloré,” says Chris Tinker of ICAP, a specialist broker. (Mr Bolloré is France's top corporate raider.) Mr Arnault and the property investors hope to extract value for investors from Carrefour's property assets, worth at least €15 billion ($20 billion). Sale-and-lease-back deals, where a firm sells property and pays rent to occupy it, generate piles of cash. But Mr Duran dislikes the idea. “Mr Arnault will seek a board seat and try to influence the company's strategy,” predicts Mr Tinker.

Internecine strife is the last thing Mr Duran and Mr Reiss need as they try to revitalise the company. To focus on countries where Carrefour is doing well, they pulled out of Japan, Mexico, South Korea, the Czech Republic and Slovakia and may yet sell subsidiaries in Portugal, Switzerland and Thailand. They have also tried to re-establish the store's reputation for low prices in France, which accounts for half its sales. On March 1st Carrefour cut the prices of its own-brand products in France by 7-8%. There are hopeful signs: net profits rose by 58% in 2006, to €2.3 billion, though most of the increase came from the sale of operations in South Korea.

But investors grumble that the company's share price underperforms those of its European rivals by a large margin. The value of the Halley family's stake has fallen by half since 1999. Until the share price recovers, the Halleys want Carrefour to stay independent. That is why they fell out with Mr Vandevelde, who had been in talks with private-equity groups about a buy-out of Carrefour without the family's consent. But in the longer run they might sell out. As founders of Promodès, another French hypermarket chain that merged with Carrefour, they are not so attached to the retailer, and have already reduced their stake from 25% to 13% of shares.

Will anyone bid for the struggling firm? Carrefour's 1999 takeover of Promodès is a deterrent, since it was the beginning of Carrefour's problems at home. Shoppers who used to go to Continent, Promodès's flagship chain of hypermarkets, defected to E. Leclerc, a rival, because they thought its prices were lower. Today, Leclerc is France's leading hypermarket, with a market share of 17%, followed by Carrefour with

14%. “I don't believe in a takeover of Carrefour,” says Jérôme Samuel, a retail analyst at IXIS Securities in Paris.

As hypermarkets in Europe and America go through a rough patch, the biggest are the most exposed. In particular they face competition from ultra-cheap discounters, such as Aldi and Lidl, which control about 40% of Germany's retail market and plan to conquer the rest of Europe. Aldi is also making inroads in America. At the same time both retail giants are under threat from Britain's Tesco, which is challenging Carrefour's dominance in Europe and is setting up shop in America. Having made the same mistakes, and facing similar problems, will Wal-Mart and Carrefour now counter-attack along similar lines?

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Brand management

Spring cleaning

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A German company tries to deal with an unwanted endorsement

RESOLVING brand confusion is a familiar management conundrum. But seldom has a company been on the receiving end of such an odd political lob as the one now in the court of Alfred Kärcher, a German family-owned supplier of cleaning equipment, with a distinctive line in bright yellow, high-pressure hosing appliances.

In the summer of 2005 Nicolas Sarkozy, France's interior minister and the leading centre-right candidate for next month's presidential election, visited a housing project in the Paris *banlieue* where a child had been killed during a gang shoot-out. Urged on by a local resident, he promised “to clean up the housing project with a Kärcher.” Mr Sarkozy said he was simply repeating the local idiom and was referring to criminal gangs. Indignant French ethnic minorities accused him of likening them to dirt. The phrase has since entered the political lexicon.

This week, nearly two years later, the company finally hit back. In a publicity campaign in France, and in a letter sent to each presidential candidate, it denounced the “recent amalgams with which its name has been associated” and warned that it had exclusive rights to the use of the brand. Kärcher is one of world's biggest cleaning-equipment manufacturers, with a range of handy appliances that includes steam cleaners, vacuum steamers, push sweepers, pressure washers and industrial cleaners. Last year it sold 6m appliances, up 10% on 2005, and worldwide turnover was €1.3 billion ($1.7 billion), up 13%.

Kärcher's French subsidiary says it has no plans to sue Mr Sarkozy for reputational damage. For the moment, its hose-down seems instead to be pre-emptive. But just how the firm intends to stop a top French politician using one of his hallmark phrases is hard to fathom. As the election looms, Kärcher may find it a lot harder to curb a politician than the spread of moss on the patio.

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Pulp and paper

Flat prospects

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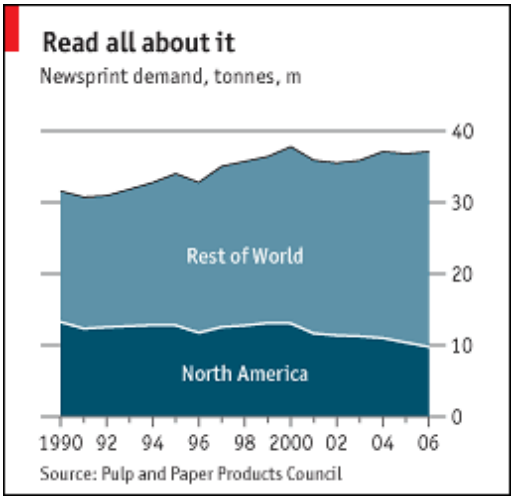
Digital media and globalisation shake up an old industry



REPORTS of the death of paper, rampant in the 1990s, were evidently greatly exaggerated. The paperless office never materialised; nor, yet, have e-books. People still print letters and flip through pages of magazines. They also eat cereal and drink milk from cartons, and wipe their bottoms with loo roll. Computers have, oddly, failed to do away with such habits.

Even so, the vast pulp-and-paper multinationals have been hard hit by the electronic age, especially in America. Demand for many types of paper there is declining, though mill closures and shrinking capacity buoy prices. Newsprint has been worst hit (see chart), as circulation and classified advertising at newspapers fall and the *Wall Street Journal* and other papers grow skinnier. North America's two biggest newsprint-makers, Abitibi of Canada and Bowater of South Carolina, are merging.

“The only grade of paper immune to technological substitution is tissue,” such as bathroom or facial tissue, says Steve Chercover, an analyst at D.A. Davidson. This week SCA, a Swedish firm, announced plans to buy Procter & Gamble's European tissue business (including the Bounty brand) for €512m ($676m), citing growth prospects of 3-4% annually.

Restructuring in the paper industry is proceeding at a furious pace. The first thing some paper companies have jettisoned is ownership of forests. International Paper (IP), one of the world's biggest pulp-and-paper companies which is based in Tennessee, used to be the largest private landowner in America. A year ago the company sold 5.7m acres, or 90%, of its forestland—an area larger than Massachusetts. The $6.6 billion sale was “probably the hardest decision that I've had to make since I became CEO,” says John Faraci, IP's boss since 2003. Most buyers were financial investors, but 5% of the land went to conservation groups.

IP is shedding entire businesses, as well as land. Gone are the company's interests in lumber and plywood (for home-building); juice and milk cartons; brown-paper grocery bags; and even magazine paper. Last month the company finished selling its North American drinks-packaging business to a New Zealand company. The company's focus is now on uncoated white paper (where growth is flat to negative in North America) and packaging.

Many other paper giants are slimming down too. Weyerhaeuser, an American lumber company in the middle of its own overhaul, just merged its “fine paper” division (ie, white and copy paper) with a Canadian rival. Smurfit-Stone, an American packaging giant, sold its consumer-goods-packaging business (milk cartons and the like) to focus on containerboard, which goes into large boxes for shipping, and corrugated containers.

As they thrash about for new direction, pulp-and-paper giants in America and Europe must also deal with the forces of globalisation. Cheap imports from South America, Russia and China are starting to arrive. Brazil, where production is dominated by plantations of fast-growing eucalyptus trees, is the cheapest place to make paper, says Edings Thibault of Morgan Stanley. China has recently gone from a net importer to a net exporter of newsprint. (Rising global competition may help persuade antitrust authorities to approve the new wave of North American mergers, notes Mr Chercover.)

At the same time, emerging economies also represent new markets that are not as hooked on e-mail as

the developed world is. At IP, Mr Faraci has his eye on Russia for production, as well as on China and Brazil. Last year IP announced a joint venture with Russia's largest forest-products company. It has also become the partner of a huge Chinese firm and did a land-swap in Brazil that “essentially doubled the size of our paper business” there, says Mr Faraci. For the moment, then, emerging markets offer hope. But BlackBerrys and Dells will not keep a low profile in Brazil forever.

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Mining

New frontiers

Mar 15th 2007 | FORT DAUPHIN AND ILAKAKA
From The Economist print edition

Madagascar is becoming an attractive mining destination

THE sleepy town of Fort Dauphin in southern Madagascar is trying to catch its breath. Lying in the least developed corner of one of the poorest countries in Africa, Fort Dauphin, also known as Tolagnaro, is accessible only by aircraft or by way of battered dirt roads. But four-wheel-drive vehicles have recently become common and locals congregate in the main square to watch cranes and lorries at work in the tiny harbour below. Hundreds of people have moved in from abroad and from other parts of the country. The town's few hotels are full and food prices and rents have doubled in the past year. Why? Because Rio Tinto, a global mining giant, has started work on a big mine just outside the town.

The project has been mulled over since the 1980s, but it was only in 2005 that rising commodity prices prompted Rio Tinto to invest $650m in what is thought to be the richest deposit of ilmenite in the world. The mine is expected to produce 10% of world supply of the mineral, which contains titanium oxide, used to make pigments and sunscreen, among other things. But first the company, in a joint venture with the government, which is keen to attract foreign investment after decades of isolation, must build roads, a new port and power and water infrastructure. Some of this should benefit Fort Dauphin, which lacks running water and reliable electricity. The mining giant has also been helping to educate locals about HIV/AIDS.

Others are taking a keen interest in Madagascar, too. A consortium headed by Canada's Dynatec is ploughing $2.5 billion into a nickel and cobalt mine; South Africa's Exxaro hopes to develop another ilmenite deposit; Alcan is said to be looking at bauxite deposits near Fort Dauphin; several small firms are hunting for platinum, gold and uranium; and Exxon Mobil and others are looking for oil, both onshore and off, though the prospects are unclear.

Madagascar also sits on rich gem veins, which have prompted impoverished locals to try to grab a piece of the action. Jean-Noël Andrianasolo is one of them. In 1998 he left his wife and children and headed south to look for sapphires. He was not alone. The rush has now turned an isolated savannah bordering a national park into a settlement known as Ilakaka. Along the main road, gem dealers from Sri Lanka and Thailand have set up shops and a few brick buildings have appeared among the wooden shacks.

Mr Andrianasolo struck it rich, but most did not. At the local market, mud-caked informal miners with calloused hands peddle stones in aspirin bottles or plastic bags to local dealers barely better off themselves. A few miles away, miners dig precarious 10-metre-deep pits in the sandy ground to get to the sapphires. Sometimes they are buried alive.

The mineral bonanza could do much for the 18.6m people of Madagascar, where the average income is $290 a year. Mining and oil, which make up less than 4% of GDP today, could account for three times that by 2011. But some fear mining will lead to corruption and political tension, and damage the country's unique ecosystem. President Marc Ravalomanana, a business tycoon who was re-elected in December, seems determined to avoid these pitfalls. Murky allocations of exploration permits have given way to a more open system, and new laws have created more favourable and predictable investment conditions. Gem smuggling has declined, and a world-class gemology and gem-cutting school has been set up to boost the value of exports. The government hopes to join a global initiative promoting transparency in extractive industries before large-scale production starts.

Martin Nicoll of WWF, an environmental group, reckons that mining is not necessarily incompatible with preserving the environment. In 2003 the government decided to triple the area of protected forests and big Western mining firms are keen to be seen doing their bit. In fact, slash-and-burn farming, not mining, is responsible for most of the damage. As Madagascar does its best to shake off years of ill-management and Marxist policy, the real test is yet to come: for all its good intentions, will the government be able to

stand upright when the money starts flowing?

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Face value

Nasdaq's nemesis

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From The Economist print edition

AP

Dave Cummings wants to shake up America's stockmarket duopoly

WHEN NASDAQ's advances were spurned by the London Stock Exchange earlier this year, a lack of subtlety was said to have contributed to its failure. Yet a decidedly unsubtle approach has done wonders for Dave Cummings. Mr Cummings runs BATS Trading, an electronic network that in less than two years has become America's third-largest stockmarket behind NASDAQ and the New York Stock Exchange (NYSE). BATS has captured around one-tenth of all trades in NASDAQ-listed securities and, as a result, has won the attention of big brokers. Last week Merrill Lynch joined Lehman Brothers, Credit Suisse, Morgan Stanley and others as an investor. BATS—which stands for Better Alternative Trading System—has "an excellent chance of achieving critical mass," says Michael Bleich of Lehman, because it is fast, cheap and efficient.

A self-styled computer geek who cuts an unimposing figure, even when wielding a baseball bat emblazoned with the BATS logo, Mr Cummings nevertheless considers himself to be locked in an almighty struggle. His chosen enemy is NASDAQ's boss, Robert Greifeld. Mr Cummings calls him "Bob the Bully" and accuses him of turning his exchange into a "monster" that has sought to squash competition so it can raise prices. He is, he says, happy to be thought of as the "Anti-NASDAQ". The rival exchange is the perennial target of the caustic e-mails that Mr Cummings fires off each week to a group of 1,500 devoted subscribers, including managers of rival exchanges.

The latest missive mockingly compares NASDAQ's two price cuts since January to a "blue-light special" at Kmart, a department-store chain that has seen better days. Mr Cummings likes to think they were a panicky response to BATS's latest market-share grab, an offer to abandon the usual fees and pay brokers to send business its way throughout January. NASDAQ derided the move, which cost BATS $6m, as irrational. But it worked: a lot of those who switched to the network have stayed with it. Volume averaged over 300m shares a day for the first time in February.

BATS's supporters say it is about more than gimmicky offers. It marries financial and technological expertise. Mr Cummings, who is 38, has a computer background but cut his teeth trading wheat futures, after being told he would make a lousy stockbroker. After leaving the pit he set up a firm, Tradebot Systems, to develop software that replicated what floor traders did, only better and faster. Mr Cummings thus became a leading proponent of algorithmic, or "black box" trading, in which computers decide when to buy and sell securities, eking profit out of momentary pricing anomalies. This type of trading is increasingly important for banks and hedge funds.

Two other things give BATS an edge on price. One is what Mr Cummings calls the “Halfway to India” strategy. Being based in Kansas City means his firm can pay its eggheads much less than if they lived in New York. BATS was able to grow rapidly last year while investing a mere $8m. Cheap its systems may be, but they are also stable, experiencing no problems during the recent market turmoil. The other advantage is its structure. Mr Cummings sees BATS as a “semi-profitable utility”—what NASDAQ and the NYSE were before they “got greedy” and went public. Its customer-owners see it as not only a low-cost alternative, but also a way to keep the big exchanges from the temptation of price hikes. The NYSE has not cut its prices, but with BATS now trading NYSE-listed securities too, it will come under pressure to do so.

Fans of BATS say it is merely playing the big exchanges at their own game. When Mr Greifeld took over at NASDAQ, after all, he vowed to hit rivals hard on price. Yet although tussling with a similar-sized rival is one thing, being outsmarted by an upstart run on a shoestring is quite another. Some NASDAQ executives are loth even to mention BATS by name; when they do, they refer to it as a mere “matching engine”. It is true that NASDAQ does much more than its rival, such as listing shares, licensing indices and charging for data services (some of which, Mr Cummings gripes, were free before NASDAQ bought the firms that developed them). But BATS also wants to be a full-fledged stock exchange and is putting in an application with regulators.

The dangers of success

Though Mr Cummings has done remarkably well in a short time, he has yet to prove that his low-price model is sustainable. He has nimble rivals of his own to worry about, such as Direct Edge and the latest entrant, CBSX, based in Chicago. He also faces potential conflicts of interest: Tradebot could, in theory, take advantage of BATS's proprietary information, though it is managed by a separate team. But perhaps the biggest threat stems from BATS's success. Sceptics think it will suffer the same fate as other electronic networks that have proved their worth—such as Archipelago and INET—and will fall prey to one of the big two. Or perhaps London will swoop—an intriguing possibility since it would leave NASDAQ, which owns a stake in the London Stock Exchange following its aborted bid, with an interest in BATS.

Others think BATS could become a buyer itself. Mr Cummings says a merger with a regional exchange is an option. He is already talking with Liquidnet, the number-one network for big “block” trades, about a tie-up. His aim, he says, is to overtake NASDAQ within two years, helped by new rules that will force trades to be routed to the venue offering the best price. That seems optimistic, as NASDAQ is hardly standing still: it has captured over 20% of all trading in the NYSE's ten biggest stocks. Another ambition is to expand into Europe. He recently used his weekly e-mail to offer a baseball bat and the possibility of a job to the reader with the best ideas on how to do this, and received over 50 replies. Mr Greifeld might be only too happy to see his tormentor's attention shift across the Atlantic. Perhaps he should offer some thoughts of his own.

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Family capitalism

Our company right or wrong

Mar 15th 2007
From The Economist print edition

Brett Ryder

Founders and their families often exert extraordinary power over public companies, even when they own only a minority of the shares

IN MID-2005 few investors in Porsche would have guessed that only 18 months later their firm would be the dominant shareholder in Volkswagen. Then again, it is none of their business, because they have little say over the sports-car maker's managers or strategy. The Porsche and Piëch families have total voting control over the German firm, despite owning only half of its equity. The publicly traded shares, providing the other half of Porsche's capital, have no right to vote.

After a recent European ruling, the “VW law”, which prevents any shareholder from exercising more than 20% of the carmaker's votes, is likely to be repealed. If so, the Porsche and Piëch clans will have control of VW, because Porsche holds 27.4% of the voting shares. In shareholder democracies, as in political ones, poor turnouts mean that about one-third of the votes can grant control of a company.

That is not the full extent of the families' influence. VW has a 20% stake in Scania, a Swedish truck and engineering group, which has two classes of voting shares, one with ten times as many votes as the other. Thanks to these super-voting shares, VW has 35.3% of the votes in Scania. In other words, the Porsche and Piëch families will also control Scania, thanks to an economic stake in the firm of a mere 2%.

Almost since the first company listed on the first public market, capitalists have sought to raise money without sacrificing control. Porsche demonstrates two techniques that families and founder-entrepreneurs commonly use. First is a cascade of companies—a ploy particularly favoured by Italians—to gain control of a larger group. Each stage of the cascade amplifies the capital governed by the tiny company at the top. The second, on flotation, is to issue shares to the public with vastly inferior—or no—voting rights. Both are legal.

Porsche is an extreme example of how a family can wield great power by harnessing large amounts of other people's money. But it is not unusual. An American study concluded that 6% by number and 8% by capitalisation of quoted companies in America had dual-class shares in 2002. Only two-thirds of large European companies rigorously apply the principle that one share should command one vote, according to a Belgian study in 2005.

The European Commission, eager to create an open market for corporate control, is studying whether it

should act against them. Israel stands out for having made the even allocation of votes a requirement of listing on the stock exchange. It is a tricky balance to strike. Liberalism argues that investors and owners should be free to enter into contracts as they wish. On the other hand, sheltering families that govern a company badly impedes restructuring. Isn't that bad economics?

Sweden is the European country with the most dual-class shares: some two-thirds of its listed companies have them. The Wallenbergs, one of Sweden's most famous business families, which controlled Scania before selling most of their stake to VW, could give a master-class in their use. Their foundations own super-voting shares in Investor, a quoted investment company that they control. Then there is another layer of special shares. Investor has helped develop Swedish companies such as Electrolux, a white-goods maker, and Ericsson, a telecoms-equipment company. Most of these firms have shares with disproportionate voting rights, a slug of which Investor owns.

Some of the best-known North American companies use dual-class shares. The Ford family may no longer own the company—it has a slender 3.75% of the shares—but nobody can doubt who is in control. When the firm went public in 1956 the family's shares were converted into a special class that is guaranteed 40% of the voting power, no matter how many ordinary shares are in issue. The late Alex Trotman, who held the top job at Ford in 1993-98, used to say that to be successful, the boss of Ford needs to manage the family as well as the company.

Dual-class shares are no hangover from the past. When Google went public in 2004, its founders, Larry Page and Sergey Brin, insisted on a dual-class share structure. Google sold the public new A shares with one vote per share; its existing shares, mostly held by Mr Brin and Mr Page, became B shares with ten times as many votes per share. With around one-fifth of Google's total equity, the founders still command about three-fifths of votes, and thus retain control.

Dual shares are designed to assure investors that a known group of managers will control the company indefinitely. They shield the long-term vision and strategy of founders from stockmarket forces. At Google, they are in effect founded on the idea that Mr Brin's and Mr Page's judgment is better than that of investors—and will remain so until the firm's founding geniuses (or their heirs) decide differently. The duo clearly spelt out why they wanted such a structure, in their “Owner's Manual” for prospective shareholders:

> [It] will make it harder for outside parties to take over or influence Google...and easier for our management team to follow [a] long-term, innovative approach...[and] leave our team, especially Sergey and me, with increasingly significant control over the company's decisions and fate.

Such share structures are often set up just before a company's flotation, so you can hardly accuse owners of foisting them on unsuspecting investors. Investors pay less for shares in a company with dual-class shares than for shares in an otherwise identical company that endows each share with one vote. Their rights are weaker in a firm with super-voting shares, because they can not kick out the family. Whatever their drawbacks, therefore, dual-class shares are “fair”.

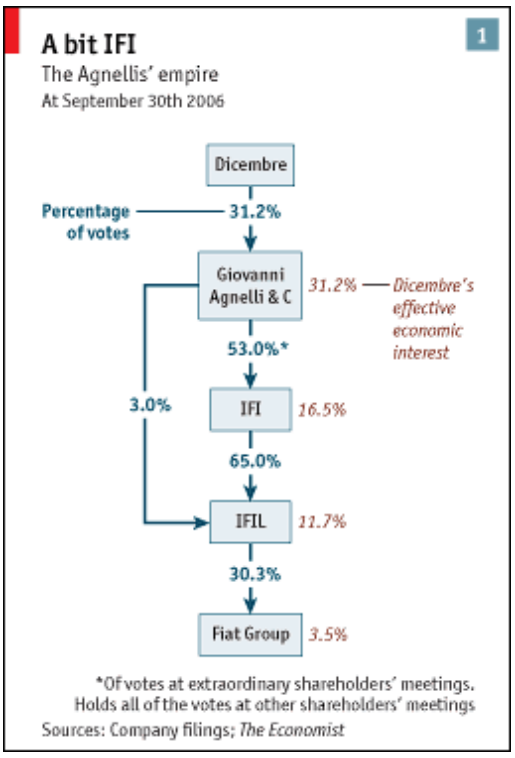
That, at least, is the theory. Sometimes, though, it seems hard to believe. Italian entrepreneurs use convoluted cascades of companies (also known as *scatole cinesi*, or Chinese boxes) to achieve the same end as dual-class shares. The company at the top of the cascade, the one that calls the shots, is usually private. This firm's controlling shareholder has enough votes to secure an absolute (or *de facto*) majority at shareholders' meetings at each level in the cascade. In effect, Chinese boxes remove control of the quoted company from its public shareholders, because the majority is fragmented into a series of minorities spread over the cascade.

This is the mechanism that the Agnelli family uses to control Fiat Group, a quoted company and Italy's largest industrial group (see chart 1). The family's *cassaforte* (literally, its strongbox), Giovanni Agnelli & C, a limited partnership, controls a 30% stake in Fiat through a cascade of two quoted companies, IFI and IFIL. This is enough to give it control of Fiat's annual shareholder's meeting. (For instance, at the meeting in 2006 less than half of those entitled to vote did so, thereby in effect doubling IFIL's votes.)

A vivid illustration of the power of Chinese boxes came in 2003 when Fiat had needed a capital increase to prop up its ailing balance sheet. It was a lesson in how to turn €250m—which the

Agnellis' limited partnership injected into IFI to pump-prime the cascade of capital increases—into €1.84 billion, which was the amount Fiat raised. In other words, the minorities in the three quoted companies in the cascade provided the majority of the money.

There is a further twist. John Elkann, a grandson and main heir of Gianni Agnelli who ruled the Agnelli's empire until his death in 2003, pulls the strings at Giovanni Agnelli & C. This is because he controls a company called Dicembre, which has 31% of the votes in the limited partnership. Tens of other descendants of Fiat's founder, none of whom speaks for more than 5%, own nearly all the rest of shares. This makes Mr Elkann's position unassailable without an unlikely alliance against him in the rest of the family. The extended Agnelli family, Mr Elkann apart, provides the capital but has no real say in what happens to it. Meanwhile, the man who controls Fiat owns a mere 3.5% of its equity.



Highly preferred stock

The economic costs of such schemes are complex. One attraction of family-run companies lies in their managers' relationship with shareholders. In most companies, managers have an interest in creaming off profits through, for instance, lavish expenses and vanity projects, rather than paying them out to the owners. By contrast family managers are the owners. The more of a family's wealth that is tied up in the business the closer the alignment of managers' and shareholders' interests. Deterring family-run companies from listing in the public markets or encouraging them to take on debt rather than raising equity might therefore be inefficient.

Super-voting shares, however, undermine this argument. Dual-class shares and cascades tempt the powerful to benefit themselves, rather than to pay money out to everyone equally. An extreme example, American prosecutors allege, is Hollinger International (now called Sun-Times Media Group), once one of the world's largest newspaper groups, with titles including the *Daily Telegraph*, a British daily, and the *Jerusalem Post*. Lord Black, its former chief executive, is standing trial this week on charges, which he denies, of siphoning tens of millions of dollars out of the firm.

The group's capital structure was a factor in the alleged frauds. Through a chain of companies, Lord Black indirectly controlled around 20% of Hollinger's shares. But he had around 70% of the votes; each of his B shares had ten times the voting rights of A shares held by other investors. Nobody could stop Mr Black from packing Hollinger's board with prominent and well-paid contacts, who seemed not to have asked too many questions. Mr Black had no counterweight, because nobody could fire him.

Despite this increased risk, calls for the reform of super-voting shares inside companies are sporadic. Perhaps this is because a company's investors know they have no chance of success without some negotiating leverage.

But when their position is strong, investors do force change. Part of the defence of Arcelor, then the world's number two steel group, against a hostile bid in 2006 from Mittal Steel, the world's largest steel group, was to criticise the bidder's governance. Arcelor's main target was the disproportionate voting rights of Mittal Steel's B shares, owned by Lakshmi Mittal , the controlling shareholder. To help his bid, Mr Mittal agreed that all shares in the new firm, Arcelor Mittal, would have equal economic and voting rights.

Another governance risk is in companies that look to the second generation for management. The worry is that Junior has got to the top thanks to Pops. This leaves no room for talented people with the wrong surname. American research suggests that second-generation companies tend to fare worse than others do.

The Lagardère family in France has found the ultimate way to pass on the quoted family firm, a magazines-to-missiles group, of which it controls just 7%. This is a French limited partnership (*société en*

commandite par actions). It has two types of partners: general partners and limited partners—the shareholders. The general partners have exclusive power to appoint the managing partners (*gérants*), who are responsible for running the business. (The *gérants* are appointed for a six-year term, which may be renewed.)

Lagardère's general partners are Arnaud Lagardère, son of the late Jean-Luc Lagardère, who set up this structure, and Arjil Commanditée-ARCO (ARCO), a company that the Lagardères control. Unsurprisingly, the general partners have appointed themselves as Lagardère's *gérants*. The firm's supervisory board, which the shareholders appoint, cannot dismiss Mr Lagardère as general partner unless he first decides to sack himself as *gérant*. And ARCO's position as general partner is untouchable so long as the Lagardère family controls it.

Doing lip service to the demands of corporate governance, the company's articles provide that shareholders approve the appointment (or reappointment) of a *gérant*. Ultimately, however, shareholders can refuse a candidate only by a majority of at least two thirds. If they do, Mr Lagardère and ARCO assume responsibility for running the business in their capacity as general partners. In other words, the Lagardère family can run the business for as long as it likes. It would lose control only if someone acquired more than two-thirds of the firm's shares and then applied successfully to the courts to change the statutes which give it control. Another of France's main companies, Michelin, the world's largest tyre-maker, is also a limited partnership of this sort.

Other French entrepreneurs or families have a less extreme way of entrenching their grip. PSA Peugeot Citroën, a quoted car company, grants double-voting rights to shares held in the same name for at least four years. The main beneficiaries of this rule are the Peugeot family: their 30% stake commands 45% of the votes.

This system was supposed to encourage loyalty in shareholders and to punish speculation. But it has mainly benefited large family-shareholders, such as the Arnaults, owners of just under half of LVMH, a luxury-goods group; their rivals, the Pinaults, who control PPR; and the Bouygues, at Bouygues SA, a construction-to-telecoms conglomerate. Martin Bouygues, one of the sons of Bouygues's founder, runs this company, just as François-Henri Pinault, one of Mr Pinault's sons, runs PPR.

The share-price discount of dual-class stock reflects the risk that the lack of control may lead to abuses. The evidence on how often that happens is mixed. For instance, a study of firms that switched from giving each share one vote to a dual-class structure concluded that on average the change was good for shareholders. Another of a sample of dual-class companies going public found that the share price of these companies outperformed comparable firms with single-class shares.

Dual control 2

Selected US companies with dual-class shares

		Super-voting shares		Controlling shareholder(s)	
	Market capitalisation $bn*	% of market capitalisation	% of total voting power		% of total voting power
Google	141.4	26.0	77.9	Sergey Brin, Larry Page	57.5
Comcast	81.4	0.3	33.3	Brian Roberts	33.3
News Corp.	73.2	32.3	100.0	Rupert Murdoch and Harris Trust	31.2
Viacom	27.7	8.6	100.0	Sumner Redstone	72.3
Echostar	19.8	53.5	92.0	Cantey and Charlie Ergen	95.8
Broadcom	18.5	13.6	61.2	Henry Samueli, Nicholas family trust	59.9
Ford Motor	14.8	3.7	40.0	Ford family	40.0
Wrigley	13.8	21.6	73.4	William Wrigley Jr.	31.1
The Hershey Company	12.6	26.4	78.2	Two Hershey trusts	79.8
IAC/Interactive	10.7	9.0	49.6	Barry Diller and Liberty Media	56.2

Sources: Company filings; *The Economist*; Thomson Datastream

*At March 12th 2007. Includes the value of super-voting shares based on price of ordinary shares if super-voting shares not traded

But the most comprehensive piece of work on the subject, a recent study by Wharton School, Stanford University and Harvard Business School of all dual-class firms from 1995 to 2002, concludes that shares with voting rights in excess of economic rights are bad for other shareholders, and that the bigger the gap the worse the damage. “What you would really like to do is give managers a lot of economic ownership in a company, but no votes, which is the opposite of what you see in most dual-class companies,” says

Andrew Metrick, one of the study's three authors. Using data from the study, *The Economist* has compiled a list of large dual-class companies, ranked by market capitalisation (see chart 2). Big media companies dominate the list and, as at the New York Times Company, occasionally attract hostility. (Full disclosure: *The Economist*, albeit a private company, has four classes of shares.)

Dutch disease

Dominant families are one thing. Managers who wield control even though they have no particular long-term interest in the company are more alarming still. The depository-receipt system in the Netherlands splits economic rights from voting rights and thereby, in effect, enables managers to have voting control without owning any share capital. When a company with this system issues shares, it does so to a voting trust, which retains the voting rights. The trust then issues depository receipts, which have economic rights mirroring those of the underlying shares.

The depository-receipt holder can tell the trust how to vote. But few holders give instructions, so the trust dominates the voting. “The voting trusts are a vehicle to get a ‘yes’ vote on every item on the agenda,” says Peter Paul de Vries, head of the Dutch Investors' Association (VEB). In 30 years of observing shareholders' meetings, Mr de Vries has not seen a trust vote against managers.

Fewer Dutch firms use the system these days. But the 10% that still do include ABN Amro (under siege from hedge funds) and ING, two banks, and Unilever, a consumer-goods giant. ING claims, as do others, that depository receipts prevent a minority from taking control. But the VEB is fiercely critical of the system, mainly because it deprives shareholders of influence. “A dictator will rarely do away with his own dictatorship,” says Mr de Vries.

The Dutch system is perverse, but other systems of control are more finely balanced. Families understandably want to keep control. On the other hand, there is a whiff of inconsistency about a family seeking public-market funds, but having such little faith in investors that it requires protection. Moreover, what looked like a good idea at the time of the company's listing might not seem so clever five decades on. At Ford, Henry's memory has been eclipsed by his descendants' endless struggle with decline.

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Global imbalances

Sustaining the unsustainable

Mar 15th 2007 | LONDON AND WASHINGTON, DC
From The Economist print edition

Satoshi Kambayashi

Global investors are worried about many things. Why is America's current-account deficit not one of them?

SOUR subprime mortgages, sluggish retail sales, the spectre of a broader retreat in credit and consumer spending. These are the American shadows that spooked investors across the globe this week, once again sending share prices tumbling from Manhattan to Mumbai.

For years, the longest shadow of all was cast by America's imposing current-account deficit. But in these fretful times, no one seems to be fretting much about the country's heavy reliance on foreign funding. New figures on released March 14th showed that Americans spent some $857 billion more than they produced in 2006, the equivalent of 6.5% of GDP, and a new record. China's trade surplus in February was the second-highest on record. It has reached almost $40 billion in the first two months of this year, three times as high as it was a year ago.

China's government, one of America's best creditors, has announced it is seeking a better return on a chunk of its foreign-exchange reserves. It will create a new investment agency, which looks sure to diversify some of the central bank's assets out of the American Treasury bonds that now dominate its portfolio (see article).

None of this had much effect on the dollar. Measured on a trade-weighted basis, it has fallen by a mere 0.04% since the recent financial turbulence began on February 27th. And as investors yawn at America's deficit, so too do policymakers. A year ago, finance ministers and central bankers from the G7 group of big, rich countries promised to take “vigorous action” to resolve the imbalances between the world's savers (particularly China, Japan and the oil exporters) and borrowers (especially America). The IMF was hoping to reinvent itself as the overseer of this grand macroeconomic bargain. A year later the venture has fizzled. The IMF-sponsored discussions between China, Japan, Saudi Arabia, America and the European Union have yielded little. They may be quietly forgotten.

What explains this nonchalance? By some measures, the world is already rebalancing. The dollar after all has fallen by 16% from its 2002 peak in real terms. Compared with the previous quarter, America's current-account deficit shrank in the last three months of 2006 and was below $200 billion for the first time in more than a year (see chart). That decline owes a lot to lower oil prices. But even excluding oil, America's trade balance seems to be stabilising as exports boom and imports slow. Even so, it is hard to

escape the conclusion that both investors and officials have become less worried about global imbalances. This is mirrored in academia, where opinion on global imbalances also seems to be changing. A few years ago most economists argued that the spectacle of poor countries bankrolling America's deficits was the perverse and unsustainable consequence of American profligacy. Economic theory suggested that capital should flow from rich countries to poor ones, and that America could not increase its foreign borrowing for ever. Empirical studies showed that deficits of more than 5% of GDP caused trouble.

Since then, economists have vied with each other to overturn this orthodoxy. Indeed, rejecting the conventional wisdom is now itself entirely conventional, as Jeffrey Frankel, an economist at Harvard University, has pointed out.

Three years ago, Michael Dooley, David Folkerts-Landau and Peter Garber, all economists at Deutsche Bank, argued that the world economy was enjoying a reprise of the Bretton Woods era. America's large external deficit could be sustained for years as Asian central banks kept their currencies cheap in order to foster export-led growth. In 2005 Ben Bernanke, now chairman of the Federal Reserve, pointed out that global interest rates were oddly low, suggesting a glut of saving abroad, not a shortfall of saving at home, was responsible for the flow of capital to America.

More recent papers have picked up similar threads, arguing that imbalances might prove to be both more persistent and less perverse than once thought. A study last summer by three economists at the IMF, for instance, showed that poor countries which export capital have grown faster than those which rely on importing it from abroad.

One reason may be the feebleness of their financial markets. That is a thesis explored by Ricardo Caballero and Emmanuel Farhi of the Massachusetts Institute of Technology, as well as Pierre-Olivier Gourinchas of the University of California, Berkeley. They point out that emerging economies have been frantically accumulating real assets, such as assembly lines and office towers, but their generation of financial assets has not kept pace. Thanks to weak property rights, fear of expropriation and poor bankruptcy procedures, many newly rich countries are unable to create enough trustworthy claims on their future incomes. Lacking vehicles for saving at home, the thrifty buy assets abroad instead. In China, Mr Caballero argues, this is done indirectly through the state, which buys foreign securities, such as Treasuries, then issues bonds of its own, which are held by Chinese banks, companies and households.

Because emerging economies' supply of financial instruments is so unreliable, people may hoard more of them as a precautionary measure. Firms and households fear they will not be able to borrow to tide themselves over bad times, therefore they choose to save for a rainy day instead. Because they cannot transfer purchasing power from the future to the present, they must store it from the past.

If global imbalances are the result of such frictions, they are unlikely to unwind quickly. Financial systems, after all, do not mature overnight. If Mr Caballero is right, America is also less vulnerable to a sudden run on its securities. Where, he asks, would the excess demand for global assets go?

So far, the behaviour of financial markets seems to vindicate his point. But, as Mr Caballero acknowledges, his thesis is largely conjectural, supported only by “spotty” academic work. And it would be a mistake to place too much faith in these new studies. If the dollar tumbles, there will be plenty of academics ready to take the old theories off the shelf and eager to say: “We told you so.”

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Buttonwood

Ponzificating

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Is the financial system a confidence trick?

CHARLES PONZI was a likeable man. That helped him persuade American investors in 1920 that he could deliver returns of 50% in just 45 days by exploiting a loophole in the pricing of international postal coupons. In a way, he was advertising an early version of an arbitrage fund.

In reality, the loophole could not be practically exploited. So Ponzi exploited his customers instead. He could deliver returns only by taking money from new investors to give to his early backers. But although he died in poverty, the Italian immigrant achieved immortality of a sort: fraudulent moneymaking operations are often known as Ponzi schemes.

In the world of finance, describing something as a Ponzi scheme is a standard form of abuse. This insult has been bandied around a lot of late. Financial-sector profits have grown far faster than GDP over the past 25 years; everyone has become richer by lending money to everyone else. Household debt is running at about 100% of GDP in America and higher still in Britain. Credit derivatives are soaring in value and payment-in-kind notes (which pay interest with more debt, rather than cash) are in vogue. Last month Tim Lee, a strategist at pi Economics, described the whole financial system as “the equivalent of a gigantic Ponzi scheme.”

In one sense, of course, he is right. Many elements of the system are Ponzi-like in that they depend on confidence—they would collapse if all investors demanded their stakes back—or they rely on new backers to keep them going. Pay-as-you-go pension systems, for example, depend on there being enough workers to fund promises made to retired employees.

The health of the commercial banking system depends on the assumption that, at any time, most depositors will keep their money in the bank. That allows banks to borrow short and lend long; earning higher rates on loans to business. When depositors panic and start to withdraw their money, the result is usually an economic catastrophe.

Ponzi's original scheme was fraudulent from the start. But even if he had found some exploitable anomaly in the financial system, his rationale was flawed. Because he offered such a high rate of return over such a short period, claims on the “Bank of Ponzi” would quickly have reached ridiculous levels.

So perhaps there are good and bad Ponzi schemes. Good schemes will do more than funnel money from latecomers to early takers, allowing the foremost to prosper at the expense of the hindmost. And they will not allow claims to increase too fast. That was the big mistake of John Law, the pioneer of paper money in early 18th-century France. Law's system eventually collapsed, but he did have the insight that the creation of credit might increase trade, and thus general welfare.

But how to tell when a scheme has gone too far? Hyman Minsky, an American economist, distinguished three kinds of borrowers. Hedged debtors can safely meet all debt payments from their cashflows. Speculative borrowers can meet current interest payments from cashflows but need to “roll over” their debt in order to pay back the principal. And Ponzi borrowers can pay neither interest nor principal from cashflows but rely on rising asset prices to keep going.

The American housing market seems to be suffering from the unravelling of a Ponzi-type system. Subprime loans were offered on generous terms that, implicitly or explicitly, depended on rising house prices. The banks that made these loans bundled them up and sold them in the credit markets to investors, eager for high yields. This was supposed to make the financial system more secure by dispersing risk more widely.

But look what is happening now. The buyers of these loans are asking the original mortgage-writers to buy them back. But these homelenders do not have the money to do so. The confidence that sustained their balance sheets has evaporated, leaving many in dire trouble.

Might the problem be more widespread than housing? The latest stockmarket wobbles suggest investors are asking themselves the same question. Financial-sector debt has risen from virtually zero 50 years ago to 100% of American GDP today, and Europe's financial corporations have helped to accelerate the money supply.

George Magnus, a strategist at UBS, has just written a research note entitled “Have we arrived at a Minsky moment?” His big worry is of a contraction in credit supply. As lending standards tighten, consumer demand could suffer, possibly prompting a recession in the United States. No one knows when the credit cycle will end, he says. But the pyramid is beginning to look a bit top-heavy.

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Big-money management

Buffettology for the Chinese

Mar 15th 2007 | HONG KONG
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Who should manage Buffett's billions? Or China's?

Get article background

WHEN Warren Buffett took over a fading textile company named Berkshire Hathaway in 1965, Mao Zedong was still plotting his Cultural Revolution, which forced anyone suspected of capitalist tendencies into crushing manual labour. From these rather different points of departure, both Mr Buffett and the People's Republic of China have arrived at a similar dilemma. Mr Buffett is now groping to replace himself as head of a company that has become, in essence, a $170 billion investment fund. The Chinese government meanwhile has yet to name the chief of its own, outsized investment fund, which will be split off from its $1 trillion-worth of foreign-exchange reserves.

Reuters

Hank Paulson enjoys Warren's wit

The predicaments facing Mr Buffett, the consummate capitalist, and the Chinese government, still avowedly communist, meet on many levels. Both are loss-averse; both have concerns about the dollar; neither can do much in Chinese currency (Berkshire by law, though it has managed to lose money speculating in yuan; China by mission). Both also suffer from their size. Whatever they hope to buy tends to become pricey because they are buying it. As Berkshire's fame and weight has increased, its returns have shrunk.

And yet, despite these handicaps, both aspire to large returns. For Berkshire, a publicly listed company, this goes without saying. It is also true for the new Chinese fund, however. Qu Hongbin, chief China economist at HSBC, says the fund will probably be charged the one-year bond rate of about 3% for the assets it manages. But because its funds will not be denominated in Chinese currency, it will also have to compensate for the appreciation of the yuan, which Mr Qu expects to be 3-5% a year. On top of that will be management costs of 1-2%. In sum, the fund may have to produce double-digit returns, which would not be that different from Berkshire's. This may cause it to hold the same kind of volatile assets, such as equities, commodities and junk debt.

Both Berkshire and Beijing share some advantages as well. Berkshire is seen as a buyer of choice, Mr Buffett says, by many owners of good, non-public companies. Dodgy governments, rich in resources and eager for loans, may likewise view China's government as a creditor of choice. Its fund may also be an attractive investor for companies seeking to do business in China. Wal-Mart, for example, a large holding of Berkshire's, is expanding in China but would probably have an easier time if the government had a stake in its success.

But Berkshire and the China fund do differ in two big ways. The first is the type of person they will employ. Mr Buffett wants an independent soul who will make contrarian calls; China is rumoured already to have chosen a fund manager who clocked up many years at its finance ministry—guaranteeing his lack of independence. A contrarian streak is a virtue on Wall Street; it can be a vice in Beijing.

The second difference is more subtle. Chinese officials suggest the fund will be expected to do “good” things, by valuing social and political returns, as well as financial ones. Mr Buffett has split these responsibilities. Berkshire's goal is to make money. If shareholders also want to do good, they can give their profits away, as Mr Buffett has pledged to do with his own. As a result, his successor has a clearer mandate and a better chance of success.

Whether China's more muddled effort can also succeed is less sure. A better approach might be to free its currency a bit, slow its accumulation of reserves and thus avoid the conundrum of how to invest them. China's government once wanted no truck with big capitalists like Mr Buffett. Now it thinks it can outdo them.

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America's capital markets

Buffettology for Wall Street

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America's finest capitalists seek to fix its capital markets

AS WELL as being rather good at making money, Warren Buffett has a talent for explaining complex problems in language any self-respecting executive can identify with. This week he got to work on the fading supremacy of America's capital markets. In the heady years before the Enron scandal, the über-investor explained, American firms, auditors and banks sliced too many shots into the rough. The job of lawmakers and regulators was to steer them back on to the fairway.

But are they now pulling shots in the opposite direction? You would think so, judging from the increasingly voluble grumbling in recent months. Two weighty reports late last year bemoaned America's loss of financial competitiveness, pinning the blame on everything from a culture of rampant litigation to the Sarbanes-Oxley law on corporate governance. This week, the noise reached a new pitch. First, on Monday, came a third hand-wringing tome, from the US Chamber of Commerce, a business lobby group. On Tuesday Hank Paulson, the treasury secretary, assembled an all-star cast for a conference. And for anyone hungry for more, the Chamber put on a brainstorming session of its own on Wednesday, featuring Barney Frank, the head of the House finance committee. America remains home to the world's largest and most liquid markets. But its lead is narrowing, worries Mr Paulson. This is partly due to financial improvements elsewhere, but also because of homegrown mistakes. He has made reform a top priority. His conference—which featured, among other luminaries, Mr Buffett, Alan Greenspan, Michael Bloomberg, Jeff Immelt, Arthur Levitt and Robert Rubin—focused on three areas of concern: regulatory structure, accounting and corporate governance.

Mr Paulson wants regulators to adopt a softer, more prudential system. It should rise above a “rules-based mindset that asks ‘Is this legal?'” and relies more on a “principles-based approach that asks ‘Is this right?'” There is, he added, not enough analysis of the costs and benefits of new rules. Moreover regulators have opted for expansion over efficiency.

Although the panellists agreed with this, by and large, they had priorities of their own. The Sage of Omaha railed against the pointlessness of much of the work done by audit committees (while joking that he does not get asked onto compensation committees because they prefer Cocker Spaniels to Dobermans). Mr Immelt chose to focus on the incomprehensibility of accounting rules. Mr Greenspan mused on the inherent inflexibility of financial regulation. Mr Levitt, a former head of the Securities and Exchange Commission (SEC), and Mr Rubin, who used to have Mr Paulson's job, sparred over the class-action culture, the former seeing it as broadly good for investors, the latter as bad for everyone except lawyers. Mr Bloomberg, the mayor of New York, bemoaned America's restrictive visa policy, which is depriving financial firms of talent. There was, oddly, scant discussion of the two most provocative proposals in the Chamber of Commerce's report: to end quarterly earnings guidance (so listed firms can think more long-term) and to reorganise the SEC.

Investors treat these chin-wags with some scepticism. Where, they ask, is the discussion of America's poor shareholder rights compared with Britain's? Company owners have no vote on pay, for instance. Wall Street's banking giants are more indifferent than frustrated. As they become more global, their home market's fate seems less important to them. Goldman Sachs reported record quarterly profits even as Mr Paulson and his high-powered friends were gathering in Washington.

Others wonder whether America really does have much to worry about. Sarbanes-Oxley's heavily criticised section 404, on companies' internal controls, is already being loosened. The SEC is looking into a more principles-based approach to policing markets. Despite the much-lamented decline in initial public offerings, America still leads by a country mile in merger advice, hedge funds and so forth.

Indeed, it could do more to trumpet its strengths. Some of the firms listing in London and Hong Kong

were unable or unwilling to meet the listing requirements of American exchanges. Those requirements generate a share-price premium over other markets (albeit one that has fallen a bit). Mr Levitt says he is sick of hearing about the strengths of Britain's Financial Services Authority. He doubts it protects investors as well as its American counterpart.

Besides, no one expects big reforms soon. Bob Steel, a treasury under-secretary, accepts that on some issues the talking is likely to go on for years. Which leaves plenty of time for more conferences, more reports, and more slices and pulls.

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Mutual funds

Hedge-fund envy

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Mutual funds borrow a few ideas from hedge funds

MUTUAL funds are the familiar, unexciting face of stockmarket capitalism, the financial product of choice for millions of investors. But a growing number of mutual-fund managers, including some old hands, are now borrowing investment strategies from the smaller, younger and sharper world of hedge funds.

Even the names of their products are being spiced up: Global Alpha Edge, a new fund offered by State Street Global Advisors sounds like it was dreamt up by a hedge fund. In fact, it is a mutual fund employing a "130/30 strategy" (a blend of long and short positions, betting that certain stocks will rise and a select few will fall) allowed under new European rules.

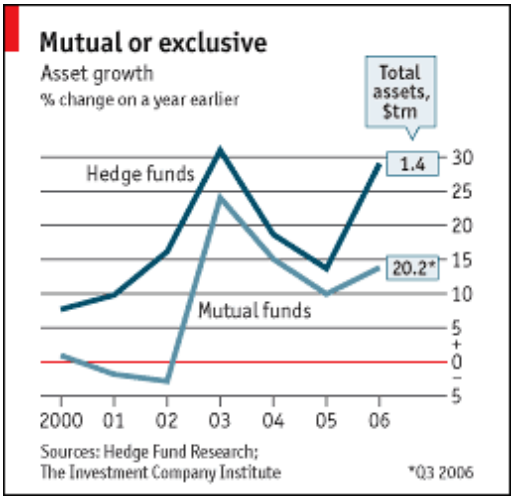
Todd Trubey of Morningstar, a rating agency, distinguishes three sorts of mutual funds that show hedge-like characteristics. Some funds, which describe themselves as "market-neutral", aim to make money in bad times as well as good. But it is hard, Mr Trubey says, to wring worthwhile returns from such a strategy without the leverage hedge funds use.

A second, far more ambitious strategy is the "equity long-short" approach. This involves bets on the direction of individual stocks. Shorting stocks—betting they will lose value—is a dicey game that can pay handsomely for some and fail miserably for others.

Other products offer the "fund-of-funds" approach, which combines a number of strategies in a single product. Some invest in a range of hedge funds. In others, mutual-fund managers get access to special accounts set up for them exclusively by hedge-fund managers, offering exposure to some of their strategies without all of their leverage.

Unfortunately for investors, this financial engineering comes at a price. The notoriously juicy fees earned by hedge funds are creeping into the mutual-fund world as well.

Thus far, these racier products account for only a tiny share of the $20 trillion invested in mutual funds (see chart). They were inspired in part by the stockmarket collapse earlier this decade, which did not stop hedge funds showing strong returns. But ironically, they are emulating hedge-fund strategies just when overall returns to that asset class are falling.



Moreover this cross-pollination can go only so far, since the two sorts of funds appeal to different audiences and thus play by different rules. Governments want a tight regulatory leash on mutual funds, which are geared to individual investors, many of them saving for retirement. They must continually disclose information, they face restrictions on borrowing and they must typically hold a relatively liquid mix of assets (although Europe's regulators are beginning to allow freer use of derivatives, for instance). In contrast, hedge funds target institutional investors and the ultra-rich and so are free to invest creatively, change course quickly and leverage their bets heavily. Unlike mutual funds, though, they cannot market themselves to the general public.

Politicians, as well as punters, will determine the success of both kinds of funds. In the European Union, the UCITS III directive (Undertakings for Collective Investment in Transferable Securities) is meant to give mutual funds more freedom to invest. But it is being implemented at different speeds and

in different ways in various countries. In France and Spain such funds are widely accepted; in Germany they are much less popular. Meanwhile, in America congressional hearings on both mutual funds and hedge funds are underway, including a proposal to limit access to hedge funds to investors with at least $2.5m to their name. Hedge funds may enjoy great freedom to pursue whatever strategies they like. But they must envy the freedom of mutual funds to chase any customer they choose.

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Vietnam's stockmarket

The South China Sea bubble

Mar 15th 2007 | HO CHI MINH CITY
From The Economist print edition

Deterring a new foreign invasion of Vietnam

THE trading floor at Saigon Securities in Ho Chi Minh City is buzzing on Monday morning, as shares edge towards another record closing high. Hundreds of investors watch the big-screen display of prices; their eyes fixed on their stocks, their ears fixed to their mobile phones.

Like many locals, Nguyen Kim Dinh and his wife now visit their stockbrokers every day. Mr Nguyen has retired from his job with the city government and plays the markets full-time. Many others, to their bosses' consternation, slip out of the office or spend all day checking their portfolios on the internet instead of working. A sneak peek has been especially tempting of late: the main VN Index, which rose by 145% last year, was up by a further 56% by March 12th, though since then the worldwide market jitters have brought Vietnam's shares off the top.

Squeezing past the tip-sheet sellers crowding the stockbroker's doorway, Mr Nguyen leads the way to a café next door, where spivvy characters in baseball caps are touting shares in obscure, unlisted companies. One, whose business card describes him as “CEO” of a one-man broker, is touting a block of shares in a hydro-electric firm for the equivalent of $22,000. How can we find out about this company, Mr Nguyen asks? No problem, smiles the broker, I can put you in touch with people who work inside it.

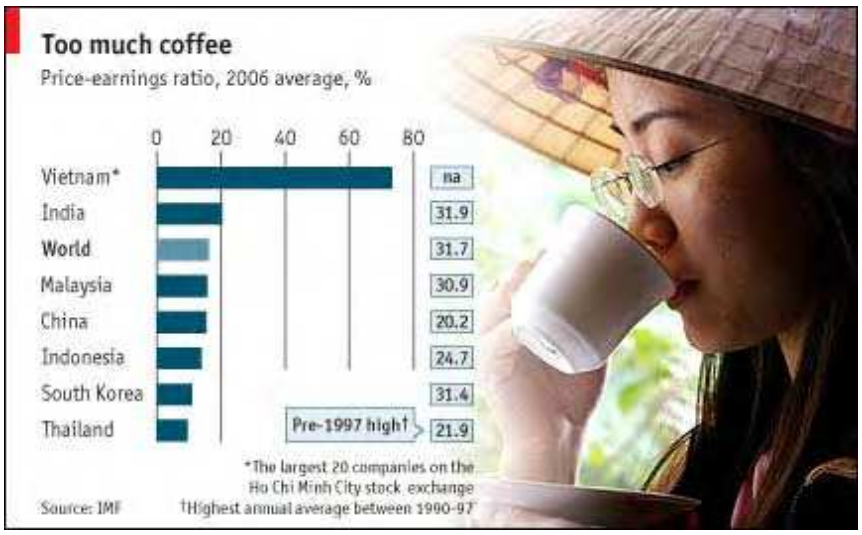
Insider trading and worse frauds are a grave danger on this “OTC” (over-the-café-table) market. But risks are not much lower on the official exchange. Many firms, including state companies up for privatisation, are only now starting to keep proper, audited accounts. The State Securities Commission is struggling to keep up with the flood of new listings. Reliable information is scarce, making it easy to whip up prices by spreading rumours. Last week shares in a broker soared when it hinted it had agreed on a link-up with Wall Street's mighty Goldman Sachs, then plunged when this proved untrue.

The popular embrace of share-trading is all the more remarkable given that the stockmarket did not exist until seven years ago. The bullishness is partly justified. Vietnam has enjoyed annual growth of around 7-8% since 2000. Perhaps $20 billion of foreign direct investment is expected this year, which should keep the economy humming. The government, though still nominally communist, has quickened its free-market reforms, recently joining the World Trade Organisation. Hidden horrors there may be, but some firms also have hidden treasure, notes Dominic Scriven of Dragon Capital, a local investment bank. In particular, land is often valued on their books at well below market prices.

Even so, the impromptu trading rooms of Ho Chi Minh City are beginning to resemble the London coffee-houses that incubated the ruinous South Sea Bubble in the early 18th century. Mr Nguyen reckons his fellow punters do realise that prices can go down as well as up—though some of those crowding the trading floor look as if the shirts on their backs are the only ones they have to lose.

Although much of the buying is local, foreign investors are also piling in to what remains a fairly small market. Its total worth has risen from $400m in early 2006 to around $22 billion. Vietnam's government and the International Monetary Fund worry that if foreign investors took fright, the market could collapse. The IMF is urging the government to cool the market, but preferably not through panic measures like the sledgehammer capital-controls that Thailand introduced last December. These triggered a stockmarket fall without achieving their objective of stopping the baht from rising.

Reuters



The IMF reckons that the price-earnings (p/e) ratio of the market's top 20 firms is 73.3—way above anything seen in other emerging markets, now or during the Asian boom that ended almost a decade ago (see chart). Local brokers dispute the IMF's sums: they say the market average p/e is “only” about 30-40. Calculations are distorted by the rush of rights issues, which is diluting earnings, thus making p/e ratios look especially giddy. If companies spend their new capital profitably, their earnings will pick up, their price multiples will fall and the market will look better value.

So far, the authorities have been cautious, says Alain Cany, HSBC's chief in Vietnam. He expects measures to slow, but not obstruct, flows of foreign portfolio investment. Local banks, which have been lending freely to finance share-buying, are being reined in—though Mr Cany thinks the restrictions should be even tighter. Taxing capital gains, as the government has contemplated, would also cool the market. Perhaps most importantly, the government is pressing the biggest and best state firms, which have yet to be listed, to speed up their plans. Since investors seem desperate to buy, it is best that they be offered shares in well run firms with good prospects. Give the running dogs of capitalism something to leap at.

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Economics focus

Small loans and big ambitions

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The commercialisation of microcredit and what stands in the way

COMPARTAMOS may not be the biggest bank in Mexico, but it could be the most important. Established in 1990 as a non-profit group making small, uncollateralised business loans to the poor ("microcredit"), Compartamos today reaches over 612,000 clients. It also turns a profit. It is one of the few microlenders rated by international credit-rating agencies, which has allowed it to issue bonds. Last June Compartamos received the green light from the Mexican government to convert into a bank. It is so well run that bankers whisper about a possible public listing.

Microfinance, like Compartamos, has made huge strides in the past two decades. Having started as a foundling industry nurtured by charities, it then won the backing of the big international financial institutions (IFIs), such as the World Bank and the European Bank for Reconstruction and Development. Today it spans thousands of microfinanciers serving 40m individuals. Like Compartamos, many lenders now seek a profit.

Commercialisation is changing microfinance—and stirring debate. Some believe microlenders have no business making money from the poor. In many countries various rules, like interest-rate caps, have been put in place to crimp the industry's growth. This is despite ample evidence that where there is healthy competition in microlending, as in Bosnia and Peru, interest rates tend to drop substantially.

Most experts in IFIs and elsewhere believe the for-profit sector must play a role. Microlenders that can attract commercial funds—deposits, loans, the capital markets—have the potential to become self-sustaining, rather than relying on the charitable instincts of others.

Socially responsible investors are already pouring in. And even the purely profit-minded have begun to open their wallets. According to a study of 200 microlenders by MIX, which collects data on the microfinance industry, commercial funding grew to $7.3 billion in 2005, from $4.9 billion two years before.

What stands in the way of more for-profit investment from the private sector? Some banks, particularly big, international ones, shy away, fearing that profiting from the poor could smack of exploitation. An obstacle in some poor countries is the lack of a regulatory framework that would help microfinance thrive. In some places microlenders need to raise $50m or more to become deposit-taking banks, for example. In Venezuela, Argentina and elsewhere the government is making noises about jumping in with subsidised microloans, which could put profitable microlenders out of business.

Paradoxically, microcredit's biggest backers, the IFIs, may also be an impediment to its further evolution, according to a recent controversial study by a microfinance consultancy and MicroRate, a microfinance ratings agency*. The paper finds that IFIs concentrate their loans on the big microlenders that do not need them, pouring 88% more money into these groups in 2005 than they did in the previous year. This crowds out commercial investors, argue the authors. Many bankers agree, noting that IFIs often tie other handouts to loans and undercut commercial lenders by up to 3%.

The problem is acute, because only around 300-400 of the world's 10,000 microfinanciers are as yet "investable", argues ACCION International, a microlender. The rest of them lack the capacity and expertise to take investors' cash. According to the Consultative Group to Assist the Poor (CGAP), a consortium of development groups, investors can choose from 74 microfinance funds, which channel investment to the sector. But a quarter of this investment flows into just ten of these funds.

Why would IFIs get in the way? The authors claim that these groups, which have an urge to lend and spend, have grown lazy. Investing in a handful of large microlenders is easier than making dozens of smaller loans to untested, fledgling ones. It is also safer and more profitable. This bolsters the donors'

own balance sheets and also strengthens their case whenever they must convince sceptical finance ministries and taxpayers that their largesse does yield results.

Killing them softly

Not all IFIs are guilty of course—and even the “guilty” ones do good work in other areas. But the problem, says Don Terry of the Inter-American Development Bank, is real. “We and others have proved the model works. Now it's time to move on. Our job is to go where others won't, not where they will.” The bank is selling its stakes in successful MFIs. Indeed, it exited the first microfinance debt fund, which it helped create, three years before its ten-year commitment ran out, because there was so much interest from the private sector.

Success has many financiers

Characteristics of a sample of microlenders (rated by MicroRate)
2005

	Credit rating			
	Alpha	Beta plus	Beta	Beta minus
Average portfolio of microloans, $m	50	14	9	11
Average RoE, %	28	22	13	15
Average IFI* debt, $m	2.1	1.3	0.6	0.1
Average increase in IFI debt, %	88	12	nil	-25

Source: MicroRate *International Financial Institutions

Although the MicroRate paper fingers IFIs, some argue that irresponsible lending by philanthropists is just as harmful. They, too, can crowd out for-profit money and, more importantly, local deposits which provide sustainable funding, and also a safe place for the poor to save. Foreign money, public and private, can provide an “important stop-gap”, says Elizabeth Littlefield, chief executive of CGAP, but “I worry that it is not necessarily catalysing the creation of a sustainable, savings-based financial system in poor countries.”

Still, the transformation is happening in snippets, particularly in Latin America. Pichincha, Ecuador's largest bank, established a microfinance subsidiary in 1999 with backing from an American development agency. Today the subsidiary contributes 12% of Pichincha's total profits, with arrears of less than 2%—while providing loans to the poor at competitive rates. Citibank houses its microfinance transactions in its bank, not in its community-development group, as others do.

The turning point will come, according to Ms Littlefield, when microfinance is seen not as a new asset class—which “ghettoises” the poor—but as the newest product line for retail banks. The industry has already transformed itself once, from a financial curiosity to a *cause célèbre*. In so doing, it has created millions of micro-capitalists in poor countries. Now it needs to attract throngs of big capitalists from rich ones.

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* “Role Reversal: Are public development institutions crowding out private investment in microfinance?” by Julie Abrams and Damian von Stauffenberg

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The Marjorie Deane internship

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Applications are invited for the 2007 Marjorie Deane internship. This award, financed by the Marjorie Deane Foundation, is designed to provide work experience for a promising journalist or would-be journalist, who will spend three months of the summer at *The Economist*, writing about economics and finance. Applicants may also be considered, if they wish, for an internship of similar duration at *CFO Europe*, a sister publication of *The Economist*. Applicants should send a letter introducing themselves, with an original article of no more than 650 words that they think would be suitable for publication in this section of *The Economist*. Applications should be sent by e-mail to deaneintern@economist.com or posted to the Business Affairs Editor (Deane internship), *The Economist*, 25 St James's Street, London, SW1A 1HG. They must reach us by April 13th.

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Evidence-based ethics

Logical endings

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Computers may soon be better than kin at predicting the wishes of the dying

Alamy

IN 1947 a psychologist called Theodore Sarbin made a controversial suggestion to a medical conference. He proposed that a doctor is really just a machine whose purpose is to make actuarial judgments about the best treatment for a patient. And not a very good machine, at that, for Sarbin also suggested that medicine would benefit if “we could replace [the doctor's] eyes and brain with a Hollerith machine”.

It was a remarkably prescient vision. The idea that Hollerith machines (or computers, to give their modern name) might sometimes be better than doctors at deciding how to treat a patient is now universally accepted. A computer program is, for instance, sometimes used to recommend whether the horrors of chemotherapy are likely to outweigh its blessings.

When machines trespass into the area of medical ethics, though, hackles rise. Here it is not the doctor that is being second-guessed, but the patient's relatives. The question is, if you were in a coma, whom would you more trust to come to the conclusion that you would want: your spouse or a machine?

David Wendler, of the National Institutes of Health in Bethesda, Maryland, and his colleagues have looked into this question. Their answer, just published in the *Public Library of Science Medicine*, is surprising. At the moment, both are equally reliable—but only the machines are likely to get better at it.

Dr Wendler's study began last year, when his team reviewed all the experiments they could find that had attempted to test how well people predict the wishes of patients with life-threatening conditions. Some of these studies used real patients whose conditions might have led them to fall into a coma—when, obviously, they could not make the decision for themselves. Others employed surrogates who were asked to make “living wills” outlining their preferences for treatment (or the lack of it) in various hypothetical circumstances. The desires expressed by these patients, whether real or surrogate, were then compared with what those patients' kin predicted the patients would want, and also with the predictions of unrelated people (doctors, for example) who might be called on to make the decision if kin could not be found.

Dr Wendler found 16 published reports containing almost 20,000 pairs of decisions. His analysis showed that kin and patient agreed only 68% of the time. When they did not agree, kin were more likely to recommend treatment when the patient wanted treatment withdrawn rather than mistakenly to recommend withdrawal. Surprisingly, the bias towards treatment was equally strong when the decision

was made by an unrelated person such as a doctor.

Other research has suggested that the variable most reliably governing whether a patient would want the machine turned off is the “1% rule”. This is that people seem to want life-saving interventions if there is at least a 1% chance they will recover the ability to reason, remember and communicate. Less than 1%, and it is time to pull the plug.

Calculating will

Using that rule of thumb, Dr Wendler and his colleagues wrote a computer program that assesses the prognosis for a patient, based on the sort of clinical criteria that the studies had described to both patients and predictors. Only 12 of the 16 original studies contained sufficient detail to be used, but the result was remarkable. In these 12 studies, human predictors guessed the patient's wishes rather more accurately than was true when all 16 were lumped together—getting them right 78.4% of the time. Dr Wendler's program achieved an almost identical result—78.5%.

Since that result is based on a single criterion, the 1% rule, Dr Wendler reckons he can beat it by adding other factors to the program. Older patients may be less willing to accept heroic, invasive surgery than younger ones; men might think differently from women; professors imagining themselves with advanced dementia may more readily turn down pneumonia treatments than dancers would. Dr Wendler's guess is that by studying such preferences in more detail and adding them to the program, he might increase its accuracy by as much as another ten percentage points.

At the moment, such data do not exist. No one has yet had a reason to collect them. But they do have a reason now. The decision about when to pull the plug on a patient who is not expected to recover is unlikely ever to be handed over completely to a machine. But when no kin can be found, the program's opinion might help. And even when a dying patient is surrounded by people who care about him, those people may welcome some guidance about what his wishes were likely to have been. Individuals are, indeed, individual. But that does not mean their dying wishes are all that different.

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Flu vaccination

Pricking consciences

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From The Economist print edition

What is good for the individual is not always best for society

MATHEMATICIANS like to play games. In particular, they like to play games that examine how people pick ways of behaving that will maximise returns. One such mathematician is John Nash, who won a Nobel economics prize for his work on the subject. He demonstrated that there are games (the most famous being known in the trade as “prisoner's dilemma”) where the players can arrive at a situation now known as a Nash equilibrium. This is the point at which no one has anything to gain by changing his strategy unilaterally. A Nash equilibrium, however, is rarely the best possible outcome; it is merely the one that pertains if the players are unable or unwilling to co-operate.

That insight has found wide application in both the social and the biological sciences. The latest example is a paper published in this week's *Proceedings of the National Academy of Sciences*, by Alison Galvani, of Yale University, and her colleagues. Dr Galvani looked at a classic example of a case where the best choice for the individual may not lead to an optimal outcome for society: vaccination.

The vaccination programme Dr Galvani studied was for influenza in America, a country where people are offered flu jabs once a year to protect them from the most severe form of the disease likely to be in circulation that winter.

Dr Galvani asked almost 600 university employees about their attitudes towards flu jabs for themselves and their families. Her survey found that people aged 65 and over were more likely to be vaccinated than other adults. From a Nash point of view, that makes perfect sense, as the elderly are at greatest risk of dying if they contract influenza. However, as the parents of any small child know, it is the young who bring pestilence into the home. Thereafter, adults spread coughs and sneezes in their workplaces. Vaccinating the young would reduce the spread of flu, thus saving lives. The researchers therefore asked whether any children living in the household had been vaccinated and found that immunisation rates for the young were lower than for adults. Again, that makes perfect Nash sense, since children rarely die of seasonal influenza.

Indeed, from a public-health point of view, the situation could be even worse. Mathematical theories such as Dr Nash's tend to assume a world populated by individuals who behave in fully rational ways, because they have perfect knowledge. Dr Galvani and her colleagues recognised that this was unlikely to be completely correct, even among people working in American universities. Their results confirmed their suspicions. People overestimated their chances of catching flu and the length of time for which the disease would be contagious, and underestimated the effectiveness and duration of the vaccine. The only aspect that most people were clued up on was the length of time for which they would suffer symptoms, which was between four and five days. Combining those findings with the other results of the survey, the researchers concluded that if their subjects were better informed, their incentives to act more selfishly would increase, and the pattern of immunisation would look even more like a Nash strategy.

The converse approach to vaccination, known as a utilitarian strategy, relies on the concept of “herd immunity”. The idea is that when a critical proportion of a group is immune to a disease, too few individuals are susceptible for that disease to be passed from one to another. A disease that cannot transmit itself rapidly dies out.

The researchers calculated that a population which followed a Nash strategy would contract 100 times more infections than one which followed a utilitarian strategy. Indeed, if 77% of young people were given jabs, seasonal flu could be all but eliminated. A utilitarian strategy, however, is a top-down affair because it relies on a community-wide programme, rather than on individuals' choices about whether to get vaccinated.

Persuading people to act in the interests of society rather than on their own behalf is likely to be harder than showing mathematically that this is the best thing to do. However, the researchers did identify a case where individual and societal interests were more closely aligned. This was a second type of influenza: pandemic, rather than seasonal, flu. When a pandemic takes hold, it kills millions of people in many different countries.

In this situation, the utilitarian strategy is also the Nash strategy. Because the disease kills the young as well as the old, parents have good reason to get both themselves and their children vaccinated. Which is a small piece of good news for those charged with contemplating how to deal with an influenza pandemic.

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Environmental genomics

Sorcerer's apprenticeship

Mar 15th 2007
From The Economist print edition

What Dr Venter did on his holidays

FOR the past few years Craig Venter, a man who annoyed a lot of people by running a privately funded version of the Human Genome Project, has been mixing business with pleasure. He has done so by sailing his yacht, *Sorcerer II*, through the world's oceans and taking samples on the way. His inspiration was the voyage of *HMS Challenger* in the mid-19th century.

That expedition was intended to sample the ocean bed and search for new forms of life there. *Sorcerer*'s grandly named Global Ocean Sampling Expedition has also been looking for new life. But it has not had to do so at the bottom of the sea, for the surface has yielded variety enough. As Dr Venter and his team report in *Public Library of Science Biology*, this one expedition has tripled the number of proteins known to science. That is a huge bounty for biologists. It is also encouraging for those who, like Dr Venter, think that bacterial enzymes are crucial to a future in which (as he sees it) a lot of energy and useful chemicals will be generated using biotechnology.

The voyage of the bounty

To understand the importance for biology of looking at microbes in the ocean, two common assumptions have to be abandoned. The first is that the most important parts of biology are those animals and plants that are visible to the naked eye. The second is that land creatures are more important than sea creatures. The truth is first that even when measured by total weight, microbes are the most important part of biology; when measured by species diversity they are incomparably the most important. Second, the oceans occupy twice as much of the Earth's surface as the land does, and have been home to life since it first came into being almost 4 billion years ago. Plants have grown on dry land, and animals scuttled there, for only about a tenth of that time. There is therefore more space and time for things to have evolved in the sea than on the land.

Biologists have focused on visible life for good reasons. Besides the obvious one that it is easier to observe something if you do not need a microscope, even keen microbiologists have difficulty growing the objects of their study in the laboratory so that they can put them under the microscope in the first place. Dr Venter gets round that problem by not bothering with it. Instead, he uses a DNA-sequencing technique that he himself developed, to get directly at bacterial genes in a sample.

Shotgun sequencing, as this technique is known, relies on blasting the genetic material in the sample into tiny pieces, and then working out the order of the individual genetic “letters” that spell out the message in each piece. (The pieces are put back together again by a computer program that matches up their ends.) The advantage of this trick is that you can use it simultaneously on DNA from many different organisms. Because of the way the reassembly program matches things up, only fragments from the same original will be joined. The result is some 6m newly identified genes (and, by implication, the proteins they describe) to add to the 3m already in the world's databases.

The consequences of this discovery will take years to assimilate, but Dr Venter does outline a few preliminary results. One of his conclusions is that even those who concentrate on bacteria may be missing the point. A larger-than-expected share of the new proteins were from viruses. Another conclusion is that if you live in the ocean, you do not need to be able to swim—at least, genes for proteins that make up the propeller-like flagella of terrestrial bacteria are surprisingly rare. Presumably there is no point in struggling against the ocean's currents.

His main conclusion, though, is that biologists have only scratched the surface of protein diversity. That

was illustrated by two things. One was a detailed study some of the team carried out on an important group of messenger-molecules called protein kinases. Biology teaches that most of these belong to a single family of proteins and that they are active mainly in animals and plants, rather than bacteria (which have been thought to rely on a different sort of molecule to do the same job). The Global Ocean Sampling Expedition suggests, by contrast, that there are 20 families of protein kinases, of which 19 are found in bacteria alone. Biological orthodoxy, in other words, has got it completely wrong.

The second illustration of how few proteins have even been found, let alone studied, is the rapid rate at which new families of proteins are being identified. If most families were already known, this rate would be tapering off—but it isn't. It may no longer be true to say that there are plenty more fish in the sea, but it does seem there are plenty more microbes.

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Consumer electronics

Mind games

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Brain-controlled games and other devices should soon be on sale

HOW would you like to rearrange the famous sarsens of Stonehenge just by thinking about it? Or improve your virtual golf by focusing your attention on the ball for a few moments before taking your next putt on the green-on-the-screen? Those are the promises of, respectively, Emotiv Systems and NeuroSky, two young companies based in California, that plan to transport the measurement of brain waves from the medical sphere into the realm of computer games. If all goes well, their first products should be on the market next year. People will then be able to tell a computer what they want it to do just by thinking about it. Tedious fiddling about with mice and joysticks will become irritants of the past.

Controlling things by mere thought is a staple of science fiction. That fiction, though, is often based on a real technique known as electroencephalography (EEG). This works by deploying an array of electrodes over a person's scalp and recording surface manifestations of the electrical activity going on under his skull.

Emotiv

At the moment, EEG's uses are mostly medical. Though the output of the electrodes is a set of crude brain waves, enough is now known about the healthy patterns of these waves for changes in them to be used to diagnose unhealthy abnormalities. Yet, because parts of a person's grey matter exhibit increased electric activity when they respond to stimuli or prepare for movements, there has always been the lingering hope that EEG might also manifest someone's thoughts in a machine-readable form that could be used for everyday purposes.

To realise that hope means solving two problems—one of hardware and one of software. The hardware problem is that existing EEG requires a helmet with as many as 120 electrodes in it, and that these electrodes have to be affixed to the scalp with a gel. The software problem is that many different types of brain waves have to be interpreted simultaneously and instantly. That is no mean computing task.

The power of thought

Both Emotiv, which is based in San Francisco, and NeuroSky, of San Jose, think they have cracked these problems. Emotiv recently unveiled a prototype headset that has a mere 18 electrodes. Moreover, no gel is needed for these electrodes to make a good contact with the headset-wearer's scalp. Emotiv claims that its system can detect brain signals associated with facial expressions such as smiles and winks, different emotional states such as excitement and calmness, and even conscious thoughts such as the desire to move a particular object. It will not say precisely how this trick is done, but it seems to work well enough

to make a virtual character in a game mimic a player's own facial expression, as well as permitting that player to move things around just by thinking about it.

To encourage others to add to this bag of tricks, Emotiv has also created a special kit for software developers. This should enable programmers to rewrite their code in a way that will allow Emotiv headsets to be plugged into existing applications.

According to Nam Do, Emotiv's boss, those applications are most likely to be single-player computer games running on machines such as Microsoft's Xbox 360 and Sony's PlayStation 3. In the longer term, though, he thinks the system will be ideal for controlling avatars (the visual representations of players) in multiplayer virtual worlds such as Second Life.

For Stanley Yang, the boss of NeuroSky, even 18 sensors seems too clunky. His firm's technology has reduced the brainwave pickup to the minimum specification imaginable—a single electrode. Existing versions of this electrode are small enough to fit into a mobile phone and Mr Yang claims they will soon be shrunk to the size of a thumbnail, enabling people to wear them without noticing.

Reducing the mind-reader to this bare minimum makes it cheap—about $20, compared with several hundred for Emotiv's headset—though it is not as precise. But that lack of precision may not matter. According to Klaus-Robert Müller, a computer scientist at the Fraunhofer Institute in Berlin who has been studying the problem for years, a single well-placed electrode is sufficient to gather meaningful information from brain waves. On the other hand, Dr Müller and his team have been unable, as yet, to produce a device that works well outside the cosseted environment of a laboratory.

There are several reasons for this. First, although human brains are similar to one another in general, they are different in detail, so a mass-produced headset with the electrodes in standard locations may not work for everyone. Second, about one-third of the population is considered “illiterate”, meaning in this context that not even a full-fledged medical EEG can convert their brain activities into actions. Third, electrical signals generated by muscular activity such as blinking are easily confused with actual brain-wave readings. Wink at a fellow player at the wrong moment, then, and you might end up dropping that sarsen you have lifted so triumphantly from the fields of Salisbury Plain on the toes of your avatar's foot.

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Chronobiology

Time and chance

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How well you can think at night may be determined by your genes

THE idea that people might be chosen or rejected for jobs on the basis of their genes disturbs many. Such discrimination may, however, be a step closer, thanks to work just published in *Current Biology* by Derk-Jan Dijk and his colleagues at the University of Surrey, in England.

Dr Dijk studies the biology of time-keeping—in particular of the part of the internal body-clock that sends people to sleep and wakes them up. One of the genes involved in regulating this clock is known as *PER3* and comes in two forms. Dr Dijk's work suggests that one of these forms is more conducive to night-shift work than the other.

The two forms of *PER3* translate into two slightly different proteins, one of which is longer than the other. Previous work by this group showed that people with two short versions of the gene (one from each parent) are more likely to be “owls”, preferring to get up late and go to bed late. “Larks”—in other words, early risers, have two long versions.

Pursuing this line of enquiry, Dr Dijk and his team have been studying how such people respond to sleep deprivation. Two dozen volunteers, some genetic owls and some genetic larks, were forced to stay awake for two days.

The genetic larks reacted to this worse than the owls did. In particular, larks given memory tests and puzzles to solve between the hours of four and eight in the morning turned in far worse performances than did owls. Their brain waves, as measured by electroencephalography, also suggested that when they were eventually allowed to sleep, they slept more deeply than owls. (Deep sleep is associated with slow brain waves, and larks spent 50% more time in such slow-wave sleep than owls did.)

What implications that may have for employers is not fully clear. As the researchers point out, this was a laboratory study, not one that involved handling the problems of the real world. Nevertheless, it is intriguing. There may yet come a time when employers running night shifts will want a blood sample from prospective employees—if only to protect themselves against negligence suits should someone have an accident.

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Correction: Satellites

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In last week's article "No hiding place" we said that the satellites of the global positioning system orbit at an altitude of 36,000km. The correct figure is 20,200km. The former is the altitude of geostationary satellites. We apologise.

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About sponsorship

Tobacco

An evil weed

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Alamy

Cigarettes may kill, but their makers know that the addiction will last

THE single most shattering statistic about life in America in the late 1990s was that tobacco killed more people than the combined total of those who died from AIDS, car accidents, alcohol, murder, suicide, illegal drugs and fire. The deaths of more than 400,000 Americans each year, 160,000 of them from lung cancer, make a strong case for the prohibition of tobacco, and particularly of cigarettes. The case, backed by solid evidence, has been made in every public arena since the early 1950s, when the first convincing link between smoking and cancer was established in clinical and epidemiological studies—yet 50m Americans still go on smoking.

Allan Brandt, a Harvard professor, has written a history of the cigarette in America. It runs from the automatic rolling machine, patented by James Bonsack in 1881, to last year's retreat by the Bush administration in a case that was intended to make the industry meet the full cost to the federal government of treating tobacco-related illness. It is a remarkable story, clearly told, astonishingly well documented ("We know more about the tobacco industry than any other business in the history of business") and with a transparent moral motif.

The Cigarette Century: The Rise, Fall, and Deadly Persistence of the Product that Defined America
By Allan M. Brandt

Basic Books, 704 pages; $36

Buy it at
Amazon.com
Amazon.co.uk

Most smokers in America eventually manage to quit, and local laws banning smoking in public have become common, but the industry prospers. The tobacco companies have survived virtually everything their opponents have thrown at them. At the end of his story, Mr Brandt writes: "The legal assault on Big Tobacco had been all but repelled. The industry was decidedly intact, ready to do business profitably at home and abroad." Although the conclusion is not to his liking, Mr Brandt's is the first full and convincing explanation of how they pulled it off.

Cigarettes overcame any lingering opposition to the pleasure they gave when American soldiers came to crave them during the first world war. War, says Mr Brandt, was "a critical watershed in establishing the cigarette as a dominant product in modern consumer culture." Cigarettes were sexy, and the companies poured money into advertising. ("More Doctors Smoke Camels", claimed R.J. Reynolds in the 1940s.) By 1950 Americans smoked 350 billion cigarettes a year and the industry accounted for 3.5% of consumer

spending on non-durables. The first 50 years of the “cigarette century” were a golden era for Big Tobacco.

That was simply because, until the 1940s, not enough men had been smoking for long enough to develop fatal cancers (women did not reach this threshold until the 1970s). The first clinical and epidemiological studies linking cigarette-smoking and lung cancer were published only in 1950. By 1953 the six leading companies had agreed that a collective response was required. They paid handsomely for a public-relations campaign that insistently denied any proof of a causal connection between smoking and cancer. This worked well until 1964, when a devastating report from the surgeon-general's advisory committee in effect ended medical uncertainty about the harmfulness of smoking.

But Big Tobacco rode the punches. When the Federal Trade Commission (FTC) ruled that health warnings must appear on each pack, the industry consented. But it shrewdly exploited the warning: “In a culture that emphasised individual responsibility, smokers would bear the blame for wilful risk-taking,” notes Mr Brandt. Many cases for damages against the companies foundered on that rock. Cigarette-makers also marshalled their numerous allies in Congress to help the passage of a law that bypassed federal agencies such as the FTC, and made Congress itself solely responsible for tobacco regulation. Describing the pervasive influence of tobacco lobbyists, he says: “Legislation from Congress testified to the masterful preparation and strategic command of the tobacco industry.”

However, the industry was powerless to prevent a flood of damaging internal documents, leaked by insiders. The companies were shown, for instance, to have cynically disregarded evidence from their in-house researchers about the addictive properties of nicotine. Internal papers also showed that extra nicotine was added to cigarettes to guarantee smokers sufficient “satisfaction”.

Despite such public-relations disasters, the industry continued to win judgments, most significantly when the Supreme Court rejected by five votes to four a potentially calamitous attack that would have given the Federal Drug Administration the power to regulate tobacco products. The industry's shrewdest move was to defuse a barrage of cases brought by individual states, aiming to reclaim the cost of treating sick smokers. The states in 1998 accepted a settlement of $246 billion over 25 years (the price of a pack rose by 45 cents shortly afterwards). In return, the states agreed to end all claims against the companies. But the settlement tied the state governments to tobacco's purse-strings; they now had an interest in the industry's success.

For those who thought the settlement was akin to “dancing with the devil”, it appeared in retrospect that the devil had indeed had the best tunes, reports Mr Brandt. To his credit, he manages to keep his historian's hat squarely on his head. But you can feel the anguish.

The Cigarette Century: The Rise, Fall, and Deadly Persistence of the Product that Defined America.
By Allan M. Brandt.
Basic Books, 704 pages; $36

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About sponsorship

Wartime espionage

Secrets and spies

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A spymistress and a mystery

BELIEVE the blurb, and Vera Atkins is a wartime heroine rescued from obscurity by an old pal. Believe her family and her story is being hijacked. “Spymistress”, by William Stevenson, a Canada-based author of books about espionage, claims she was “the greatest female agent of World War II”; Mr Stevenson is described as “her close friend...an author she greatly admired...the only person she would trust to record her life”.

Vera Atkins, who died in 2000, is certainly a fascinating figure. A meticulous authorised biography published in 2005 by Sarah Helm, a British writer, explains how she recruited and trained female agents for the wartime Special Operations Executive (SOE). Botched security—not her fault—meant many were captured and killed by the Gestapo. After the war, Miss Atkins (she never married) trekked round the ruins of post-war Europe to chronicle their fate.

But Mr Stevenson depicts Miss Atkins as far more senior: a key figure in Anglo-American intelligence co-ordination, a champion of efforts to disrupt Nazi genocide, and much more besides. These are big claims; if true, they would require the rewriting of much of the history of wartime intelligence.

That puts Mr Stevenson's sources under close scrutiny. Long-ago conversations—such as his purported meeting with Miss Atkins as a teenage messenger boy in London during the Blitz—are rendered verbatim; not a normal practice in history books. Equally puzzling is that the book's footnotes give no references for its most startling contentions. They do not detail what he says were many meetings and phone calls with Miss Atkins. He has no letters from her, he says, and wrote none; her executor (and niece), Zenna Atkins, says her aunt's papers make no mention of him; she says she heard Miss Atkins refer to Mr Stevenson only once, describing a previous book of his as “utter bilge”.

Mr Stevenson, blaming a muddle with his publisher, says he now regrets leaving out the details of his interviews with Miss Atkins from the footnotes. He is in Toronto; many of his notebooks are elsewhere. He blames the publisher also for overstating both Miss Atkins's wartime role and his friendship with her. The publisher, New York-based Arcade, blames a “concerted effort” by the Atkins family to undermine the book because of their “vested interest” in supporting Ms Helm's work.

Leaving all this aside, Mr Stevenson's book raises other issues. “Someone I knew for 40 years with blonde and then grey hair has black hair,” says M.R.D. Foot, Britain's top historian of SOE. (Mr Stevenson says Miss Atkins perhaps dyed her hair.) His book gives her middle name as Maria and her birthplace as Bucharest. Her family says her middle name was May; she was born in another town. Mr Stevenson says he was misinformed by a source, now deceased.

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About sponsorship

An African adventurer

Dark deeds

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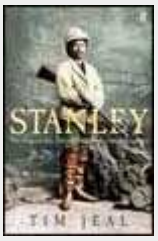
HENRY MORTON STANLEY'S reputation as a great, perhaps the greatest, explorer of the 19th century is besmirched by his association with Leopold II's grotesquely misnamed Congo Free State. He crossed Africa from east to west and then from west to east, he mounted successful expeditions to find David Livingstone and rescue Emin Pasha, and he mapped the Congo river. Yet he is now remembered mostly as the cat's paw of a Belgian king whose greed for rubber and ivory led his agents to kill or maim millions of Africans.

Stanley: The Impossible Life of Africa's Greatest Explorer
By Tim Jeal



Faber and Faber; 570 pages; £25

Buy it at Amazon.co.uk

Tim Jeal, his latest biographer, is nonetheless convinced that Stanley is a hero—albeit flawed. In seeking to justify his belief, he lays much of the blame on Stanley's family for unwittingly damaging the explorer's name. Through most of the past century they refused scholars access to Stanley's letters, diaries and other private papers. Then, still resentful that the British establishment had denied Stanley his dying wish to be buried close to Livingstone in Westminster Abbey, they sold them in batches to a museum in Belgium.

Aided perhaps by his standing as the author of intelligent biographies of Livingstone and Baden-Powell, Mr Jeal was able to persuade the Belgians to let him study the papers while they were still being catalogued at the Musée Royal de l'Afrique Centrale in Brussels. He came away persuaded that, after their famous meeting at Ujiji in 1871, Stanley shared Livingstone's vision that the spread of Christianity and commerce would halt the slave trade in Africa. More tentatively, and controversially, he also asserts that the papers are consistent with the view that, when he signed on to work for Leopold, Stanley believed that Belgium's "supremely clever" king was a philanthropist at heart.

How, though, does this assessment of Stanley square with the explorer's own lurid accounts of his bloody deeds in Africa? As a previous biographer, Richard Hall, noted in 1974 in a more readable, but less substantial, life of Stanley, the man was a chronic liar. Born a bastard in Wales and raised in a workhouse there, he denied his humble beginnings, changed his name from John Rowlands to Henry Morton Stanley and claimed the United States as his birthplace. He fought for the Confederacy in the American civil war before defecting to the Union side, from which he deserted. He then went on to tell tall tales about his wartime derring-do and about almost everything else that happened in his life. He may even have invented after the event his famous words of greeting at Ujiji: "Dr Livingstone, I presume?"

Mr Jeal finds that Stanley's imagination carried over into his journalism. He was first sent to Africa by James Gordon Bennett of the scurrilous *New York Herald*, whose readers had a mighty appetite for stories of brave white men fighting off savage Indians. Stanley sought to provide them with equivalent stories from Africa. He exaggerated the number and intensity of his conflicts there to make his copy more exciting, and these exaggerations carried over into his books. But in fact, far from being a brute, Stanley was enlightened by the standards of his day. He hated it when a black man was called a nigger, "that ugly derisive word"; he tried wherever possible to avoid bloodshed; and he showed remarkable concern for the well-being of his African followers. The Wangwana, the Swahili-speaking blacks from Zanzibar he engaged as his porters, responded by loyally agreeing to serve him again and again.

All this is plausible, but Mr Jeal strains credulity when he claims that Stanley remained unaware for so long of the rapacious African ambitions of Leopold. Others who knew the monarch much less well were not taken in. Bismarck was among them. When, in pursuit of colonial possessions, the Belgian king sent him a document expressing pious anti-slavery sentiments, Germany's perceptive chancellor scrawled a single word in the margins: "*Schwindel*".

Stanley: The Impossible Life of Africa's Greatest Explorer.
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About sponsorship

A memoir of Zimbabwe

The house that Bob burned down

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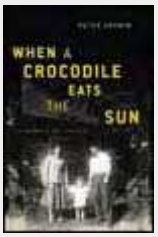
From The Economist print edition

WHAT is there new to say about the hell Robert Mugabe has visited upon Zimbabwe? Inflation exceeds 1,700%. Three million of Zimbabwe's 13m people have fled. Most of the remainder have been reduced to penury. Among them are 700,000 homeless, mostly opposition supporters, whose shacks Mr Mugabe's goons bulldozed in 2005.

It is an old story in Africa, where Mr Mugabe is but the latest model of a power-demented tyrant. His madness became clear in 2000, when, to his amazement, he lost what amounted to a referendum on his two-decade rule. Mr Mugabe turned wrecker. He promised land redistribution on a huge scale, with a programme to transfer commercial farms, mostly owned by wealthy opposition supporters, to his political base of engorged relatives, cronies and shoeless mobs-for-hire.

Commercial agriculture, which had earned about 50% of Zimbabwe's foreign currency, collapsed. Capital fled. Economic meltdown bred state thuggery and crime. The big man's solution? Last month, celebrating his 83rd birthday, Mr Mugabe pledged to remain in power at 100.

When a Crocodile Eats the Sun
By Peter Godwin



To be published in America by Little, Brown next month
Picador; 342 pages; £16.99.

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However familiar its condition, Zimbabwe's demise has grabbed the world's attention, attracting much more media coverage than bigger, concurrent crises around the continent. One reason is the tragedy of it: Zimbabwe has fallen much further than most African countries, and in a fashion of misrule that many in Africa, especially its leaders, had claimed was over. Indeed, Zimbabwe has become a litmus test of that boast. The refusal of many African leaders, especially South Africa's Thabo Mbeki, to condemn Mr Mugabe augurs ill for the continent's revival.

Another reason Zimbabwe has caught the world's eye—the main reason, most Africans would say—is that the dispossessed farmers are white. Acres of newsprint have been devoted to their troubles, even though, at around 4,000 families, they represent a small, and still privileged, minority of Zimbabwe's victims.

Peter Godwin, a Zimbabwean journalist, brings little new to their story, which dominates the first third of his book. It is rather an irritating read, often falling into the self-glamorising and self-pity that can be a feature of white Africans. “Is this how it ends?” he muses after the murder of a white farmer. “Will we be picked off one by one until those who remain just run?”

As that example might suggest, Mr Godwin is not a sufficiently original writer to give new life to an old story. With a new story, however, which he finds in his own family history, he becomes good indeed.

He discovers that his father, George, a retired engineer in Harare, is not the British émigré he has always claimed to be. He was born Kazimierz Jerzy Goldfarb, a Polish Jew, who was sent to a summer school in England in 1939, leaving behind his mother and a sister who died in Treblinka, and a father he never saw again. The book becomes Mr Godwin's quest to uncover their history, interspersed with the narrative of his parents' decline.

After decades of toil, they are ruined, their pensions and few assets worthless in Zimbabwe's collapse. Trusted servants turn on them; carjackers and thieves line up outside their gate. Their health collapses, as does the health-care system that Mr Godwin's mother, a doctor, laboured to create. The grave of Mr Godwin's elder sister, shot dead in the independence war, becomes a slum-dwellers' toilet.

Shining amid these sorrows is the aged couple's patience and great humour. After his father dies, Mr Godwin struggles with his dying wish to be cremated: the crematoriums are out of butane gas, the morgues are out of diesel. So the author has his father, a Polish Jew turned British Anglican, posthumously converted to Hinduism, and burned by the local Indian community. His mother responds to the news of this conversion: “I've always liked the Hindus,” and then wanders off to see if she has any books on Hinduism. And so, after its unpromising beginning, this ends as a rather beautiful book—about Africans.

When a Crocodile Eats the Sun.
By Peter Godwin.
Picador; 342 pages; £16.99.
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International relations

An interconnected world

Mar 15th 2007
From The Economist print edition

THE leading nations of NATO are at odds, be it over Iraq or the future role of the alliance. Russia accuses America of misusing NATO territory to advance its own missile defence. And the world's leading industrialised states struggle to set up international bodies that will regulate everything from internet protocols to the genetic manipulation of food. The experts fighting in the trenches over such issues must sometimes ask themselves: Why bother? Why create the fig leaves of international accords and institutions when, in reality, a few powerful states call the shots?

Two right-of-centre analyses address these questions in very different ways. In “The End of Alliances”, Rajan Menon, a professor of international relations at Lehigh University, does so with a bullhorn. In Rumsfeldian language, Mr Menon argues that permanent security institutions are obsolete and the United States should pick up its military toys and go home. “I believe that our alliances in Europe and Asia are dispensable.” Even worse, “they have become impediments that inhibit creative strategic thinking at home, while infantilising our partners who live under the American shadow.” What, he asks, “is the logic for deploying troops and retaining a network of bases in countries that are now wealthy enough to protect themselves...?” Concluding that there is none, he calls for the end of America's military alliances with Europe, Japan and South Korea.

Mr Menon is to be applauded for putting the issue so clearly. Unfortunately, his clear questioning is not matched by convincing, or even detailed, analysis. If Mr Menon thinks that international relations have evolved at all since the time of Hobbes, he does not admit it. Obvious counter-arguments to his view receive hand-waving dismissals. There is no need for the United States to stay in South Korea because North Korea is not really a danger, since “things are not going its way”. He predicts the North's demise without acknowledging that such predictions have repeatedly failed, or even that its death throes might be painful indeed.

If Mr Menon's book is too shrill and not analytical enough, Daniel Drezner's “All Politics is Global” is too nuanced and academic for easy reading—but ultimately much more rewarding. Mr Drezner, an associate professor of international politics at Tufts University, focuses on the international institutions and accords that regulate trade. Such regulation, though seemingly arcane at first, in fact determines “how to treat workers, how much to pollute, what can go into our food, what can be accessed on the internet,” and “how much medicine will cost”.

Like Mr Menon, Mr Drezner believes that what really matter are the domestic preferences of powerful governments: “States make the rules.” This directly contradicts Thomas Friedman's flat-world notion that globalisation has emasculated the state. Mr Friedman's ideas—such as that capitalists worldwide now form an “electronic herd” that tramples down borders—are, according to Mr Drezner, “simple, pithy and wrong”. As evidence, Mr Drezner provides case studies ranging from internet protocols to anti-retroviral drugs. He shows that “great powers cajole and coerce those who disagree with them into accepting the same rulebook.”

Unlike Mr Menon, however, Mr Drezner does not call for the end of such international accords. Rather, he finds that the challenges of the future will be increasingly transnational. As globalisation intensifies, the

The End of Alliances
By Rajan Menon

Oxford University Press; 272 pages; $25 and £14.99

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All Politics is Global: Explaining International Regulatory Regimes
By Daniel W. Drezner

Princeton University Press; 254 pages; $29.95 and £18.95

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rewards for co-ordination will increase as well. To achieve success, it is essential not to eliminate international institutions but rather to understand their utility. They are at heart a means for great nations to exert their will in concert. The key to their success lies in convincing the leading governments of the gains from acting in co-operation, rather than isolation, in a volatile but interconnected world—a message that surely applies well beyond the esoteric world of trade regulations.

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Biedermeier

The beauty of simplicity

Mar 15th 2007 | VIENNA
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Clean lines and elegance

IN THE 1980s and 1990s Biedermeier furniture—in the blond-wood style that was Germany's and Austria's answer to Georgian elegance—was much sought after. Trendy Londoners and New Yorkers bought it to furnish uncluttered flats, as the clean lines fitted that style. But it was a passing fashion. Biedermeier today sells for considerably less than it did 20 years ago, with dealers often describing furniture of the period as Viennese for fear that the word Biedermeier might lower the tone—and the price.

Their fears are hardly new. Spanning the years from the Congress of Vienna in 1815, which resolved the Napoleonic wars, to Europe's 1848 revolutions, Biedermeier struggled for recognition until well into the 20th century. Even the term (not actually used until the late 19th century) is derogatory. It was drawn from a fictional character, Weiland Gottlieb Biedermaier, whose humdrum exploits featured in an 1850s Munich satirical magazine. “Bieder” means upright or conventional. “Maier” or “Meyer” are the commonest of German surnames.

A new exhibition at the Albertina palace in Vienna suggests, however, that Biedermeier is ripe for a reappraisal. Subtitled “The Invention of Simplicity”, the show's 11 rooms display chairs, cabinets and sofas, as well as metalwork, crockery and clothing, of an astonishing delicacy.

From an exquisite Viennese chair with its back in the shape of a lyre, dated 1810, to an 1815 white-linen Austrian summer dress—surely Franz Schubert composed an early love-*Lied* to a girl wearing such a garment—to Christen Kobke's 1835 painting of a Danish castle tower, suffused with calm light, these exhibits transport the visitor back to a world of innocent contentment.

Yet historical forces at work after the Vienna congress conspired to make Biedermeier seem boring. At one extreme, Europe's cultural tastes were being shaken by the Romantic poetry of Byron, the music of Beethoven, the painting of Delacroix. At a political extreme, Karl Marx, whose theories would help shatter the post-Napoleonic dispensation, was forming his ideas just as the finest Biedermeier products were being fashioned. Meanwhile, Biedermeier was neither Romantic nor political.

Many of this show's paintings depict the familiar landscapes of Romanticism—mountains, lakes, forests and woods—but skies never glower, mountains are unforbidding and water is still. Biedermeier offers no stirrings of revolt.

The best Biedermeier paintings are interiors: indoor comfort and elegance are taken for granted, while the outdoors is both desirable and accessible. In Georg Friedrich Kersting's 1817 oil, “Woman Embroidering”, a young woman sits at a delicate table with her back to us, her right little finger raised towards an open window. The summer light this brings in illuminates her head and everything around her. The happiness of this woman (in life, Louise Seidler, a protégée of Goethe) seems eternal. The painting combines the serene leisure of a Jane Austen scene with the aesthetic intensity of a Vermeer.

The preponderance of the Albertina display is unsurprisingly towards furniture and everyday household items: sparsely ornamented tea tables and cabinets made of ash, walnut and cherry. There are chairs of a streamlined yet elegant functionality (most of the upholstery is reconstructed); and some oddities, including, from the 1820s, nine chalice-shaped, Viennese wooden spittoons.

Provincial, bourgeois: the adjectives accruing to Biedermeier might have buried it for ever. Now, in Vienna, the Albertina has brought it spectacularly to life.

“Biedermeier: The Invention of Simplicity” is at the Albertina, Vienna, until May 13th. It will be at the Deutsches Historisches Museum, Berlin, from June 8th to September 2nd and at the Louvre, Paris, from October 15th to January 15th 2008

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About sponsorship

Jean Baudrillard

Mar 15th 2007
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Jean Baudrillard, philosopher of consumerism, died on March 6th, aged 77

Corbis

AT SOME point in his career—neither date nor time being important—Jean Baudrillard took a large red cloth, draped it over a chair in his apartment, and sat on it. He may have smoked or thought for a while, or scratched his nose; a large, doughlike nose, supporting glasses. He then got up, leaving an impression of his body behind. The image pleased him: so much so, that he took a photograph.

Since he made no comment on the event (beyond the fact that the chair was later broken), the exact details are conjectural. But by putting the cloth on the chair, and sitting on it, Mr Baudrillard added to the plethora of signs, objects and symbolic acts that made up, in his philosophical system, the whole woof and warp of the 20th century. By getting up, he left behind a "simulacrum" of himself: the truth, as he teasingly put it, that hid the fact that there was no truth there. And by photographing the chair he made it "hyperreal": an image, which could be reproduced unendingly, of an object that claimed to have meaning and, in fact, had none.

Then he went to lunch.

Pourquoi pas? When a simulacrum is also a French *philosophe*, perhaps the most popular of recent decades, he needs a bottle of Merlot from time to time. And since he spent his days considering the seductive power of images and objects, it was fun to observe that he himself had such a power over the woman in the butcher's who wrapped up his *foie de veau*, just because she had seen him on television.

Whether Mr Baudrillard's world was utter nonsense, or whether it was a profound critique of a consumerist civilisation drowning in its own meaninglessness, was a matter for lively debate. Many of his French colleagues found him too much: noisy, mischievous, attached to no school (though he had sat at the feet of both Henri Lefebvre and Roland Barthes in his feverish years at Nanterre, when teaching had been interrupted by clouds of tear-gas and cobblestone-throwing). He said things that got him into trouble. His enthusiasm for the *événements* of 1968 painted him as a man of the Left, where *philosophes* belonged as naturally as fish in water; but Mr Baudrillard later broke with Marx, and called him a conservative. What he meant was that both communism and capitalism made human existence a matter of production and exchange, while he preferred to stress its symbolic side.

In any case, in his world, both the liberal and the communist narratives of history had collapsed. "The

end of history” was no longer universal capitalism and democracy or the victory of the proletariat. It was summed up for Mr Baudrillard by a lone man jogging, oblivious to his surroundings, hearing only the music of his own sound-system and aware only of the statements he himself was making: health, fashion, endurance. He was running straight ahead, but with no end in view.

The desert of the real

Of all the people he offended, none took more umbrage than the Americans. This was interesting, for he was far more popular there than in France, lecturing on various campuses of the University of California and even appearing, at Whiskey Pete's outside Las Vegas, as some sort of lounge lizard in a gold lamé jacket. In 1986 he got in a car and drove across the country, both hating and adoring it. He had never been so fully in a land of hyperreality, cluttered with meaningless symbols or, as in Disneyland, with garish synthetic versions of ordinary life. He looked for America, he wrote, in “motels and mineral surfaces...in the speed of the screenplay, in the indifferent reflex of television, in the film of days and nights projected across an empty space.” There he found himself, playing a French philosopher, roaring through “the desert of the real”.

Americans did not like his book. They did not care to be called “the only remaining primitive society”. A few years later, they objected also to Mr Baudrillard's contention that the first Gulf war of 1991 had never taken place. But, in his view, it had not. The media had created a picture of conflict; but Saddam had deployed his troops, and America had dropped its bombs, as pure statements of power in a vacuum, and the two forces had never met. General Norman Schwarzkopf, the “victor” (though with no victory) had celebrated with a party in Disneyland: QED.

All this paled, however, beside Mr Baudrillard's musings on the terrorist attacks of September 11th 2001. This was the “absolute event”, an inevitable reaction to “insufferable” American power. In the face of overweening globalisation, to destroy the twin towers was the only response. The symbol invited its destruction: “It was they who did it, but we who wished it.”

Most Americans decided, at this point, that they did not understand Mr Baudrillard very well. But then few people did. Behind the panache of his ideas—often bunkum, yet sometimes catching acutely the media-dominated triviality of modern life—the man was hidden. “No background,” he would growl, if you asked. Somewhere, there was German-speaking peasant stock and suspicious parents who wondered what on earth they had produced in this plump and bookish boy. Or perhaps there was really none of that at all: just a photograph of a suggestion of a human shape, on a red cloth on a chair.

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Overview

Mar 15th 2007
From The Economist print edition

America's current-account deficit narrowed to $196 billion in the fourth quarter of 2006, from $229 billion in the previous three months. The gap widened last year to $857 billion—a record 6.5% of GDP—from $792 billion in 2005. American employers added 97,000 workers to their payrolls in February. The jobless rate edged down from 4.6% in January to 4.5% last month.

The rate of delinquency on **American mortgages** rose to 4.95% in the fourth quarter of 2006, from 4.67% the previous quarter. The delinquency rate for subprime mortgage loans rose to 13.3%. The value of retail sales rose by 0.1% in February.

In the **euro area** industrial production fell by 0.2% in January, following a 1.2% rise in December. That left output 3.7% higher than in January 2006. Employment rose by 0.3% in the fourth quarter of 2006, a 1.6% increase on a year earlier.

Average earnings growth in **Britain** picked up from 4.0% to 4.2% in the three months to January compared with the same period a year before. Excluding bonuses, earnings growth slipped from 3.7% to 3.6%.

Consumer prices in **China** rose by 2.7% in the year to February. The trade surplus widened to $23.8 billion in February, from $15.9 billion in January. Retail sales rose by 14.7% in the first two months of 2007 compared with the same period a year earlier.

Industrial production in **Mexico** rose by 1.4% in the year to January.

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The cost of living

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Oslo remains the world's most expensive city to live in, according to the latest Worldwide Cost of Living survey by the Economist Intelligence Unit, a sister company of *The Economist*. It is now more costly to live in London and Paris than in Tokyo, which was unseated from the top spot in last year's survey. Eight of the ten dearest cities are in Europe, partly reflecting the strength of European currencies. New York, 28th of the 132 cities surveyed, is the most expensive destination outside Europe and Asia. Those looking to live on a budget should move to Latin America, which accounts for a quarter of the cheapest 30 cities. The cost of living in Buenos Aires is a little over half that in New York.

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About sponsorship

Output, prices and jobs

Mar 15th 2007
From The Economist print edition

Output, prices and jobs

% change on year ago

	Gross domestic product				Industrial production	Consumer prices			Unemployment
	latest	qtr*	2007†	2008†	latest	latest	year ago	2007†	rate‡, %
United States	+3.1 Q4	+2.2	+2.6	+2.9	+2.6 Jan	+2.1 Jan	+4.0	+2.3	4.5 Feb
Japan	+2.1 Q4	+4.8	+2.2	+2.3	+4.3 Jan	nil Jan	−0.1	+0.6	4.0 Jan
China	+10.4 Q4	na	+9.8	+9.7	+14.7 Dec	+2.7 Feb	+0.9	+2.7	9.8 2006
Britain	+3.0 Q4	+3.2	+2.7	+2.6	+0.4 Jan	+2.7 Jan**	+1.9	+2.0	5.5 Dec††
Canada	+2.3 Q4	+1.4	+2.4	+2.7	−3.3 Dec	+1.2 Jan	+2.8	+2.1	6.1 Feb
Euro area	+3.3 Q4	+3.6	+2.3	+2.2	+3.7 Jan	+1.8 Feb	+2.3	+1.9	7.4 Jan
Austria	+3.3 Q4	+3.3	+2.6	+2.5	+8.9 Dec	+1.7 Feb	+1.2	+1.8	4.5 Feb
Belgium	+3.1 Q3	+2.5	+2.1	+2.3	+3.5 Dec	+1.8 Feb	+2.4	+1.9	11.8 Jan‡‡
France	+2.2 Q4	+2.6	+2.1	+2.2	−0.6 Jan	+1.0 Feb	+1.9	+1.7	8.6 Jan
Germany	+3.7 Q4	+3.5	+2.2	+2.1	+7.9 Jan	+1.6 Feb	+2.1	+1.5	9.3 Feb
Greece	+4.3 Q4	na	+3.5§	+3.3§	+3.0 Jan	+2.7 Feb	+3.2	+2.8§	8.3 Q3
Italy	+2.8 Q4	+4.7	+1.8	+1.6	+1.3 Jan	+1.8 Feb	+2.1	+2.0	6.8 Q3
Netherlands	+2.7 Q4	+2.6	+2.7	+2.6	+4.6 Jan	+1.5 Feb	+1.1	+1.9	5.0 Feb††
Spain	+4.0 Q4	+4.8	+3.3	+2.8	+7.7 Jan	+2.4 Feb	+4.0	+2.8	8.6 Jan
Czech Republic	+5.8 Q4	+5.8	+5.1	+4.6	+9.8 Jan	+1.5 Feb	+2.8	+2.4	7.7 Feb
Denmark	+2.9 Q4	+0.6	+2.5	+2.3	+1.1 Jan	+1.9 Feb	+2.1	+2.1	3.8 Jan
Hungary	+3.2 Q4	+3.2	+2.3	+3.0	+10.5 Jan	+8.8 Feb	+2.5	+6.6	7.5 Jan††
Norway	+2.7 Q4	+2.0	+2.5§	+2.2§	−2.4 Jan	+0.8 Feb	+2.6	+2.6§	2.8 Jan††
Poland	+6.4 Q4	na	+5.4	+5.0	+15.6 Jan	+1.9 Feb	+0.7	+2.0	15.1 Jan‡‡
Russia	+6.5 Q3	na	+7.0	+6.3	+8.4 Jan	+8.0 Jan	+10.6	+7.3	7.1 Jan‡‡
Sweden	+4.7 Q4	+5.0	+3.5	+3.0	+4.1 Jan	+2.0 Feb	+0.6	+1.8	4.8 Feb‡‡
Switzerland	+2.2 Q4	+1.8	+2.1	+2.0	+8.2 Q3	nil Feb	+1.4	+1.2	3.2 Feb‡‡
Turkey	+3.4 Q3	na	+4.3	+5.3	+14.8 Jan	+10.2 Feb	+8.2	+8.3	9.6 Q4‡‡
Australia	+2.8 Q4	+4.2	+2.8	+3.2	+0.9 Q3	+3.3 Q4	+2.8	+2.6	4.5 Jan
Hong Kong	+7.0 Q4	+5.3	+5.4	+5.1	−1.4 Q4	+2.0 Jan	+1.9	+2.5	4.4 Jan††
India	+8.6 Q4	na	+8.0	+7.8	+10.9 Jan	+6.7 Jan	+4.7	+5.0	7.6 2006
Indonesia	+6.1 Q4	na	+6.0	+5.9	+23.4 Dec	+6.3 Feb	+17.9	+6.5	10.3 2005
Malaysia	+5.7 Q4	na	+5.5	+5.7	+2.3 Jan	+3.2 Jan	+3.2	+2.5	3.1 Q3
Pakistan	+6.6 2006§§	na	+6.6§	+6.0§	+6.8 Sep	+7.4 Feb	+8.0	+6.8§	na
Singapore	+6.6 Q4	+7.9	+5.4	+5.4	+14.6 Jan	+0.3 Jan	+1.8	+1.4	2.6 Q4
South Korea	+4.0 Q4	+3.4	+4.4	+4.7	+7.4 Jan	+2.2 Feb	+2.0	+2.3	3.2 Feb
Taiwan	+4.0 Q4	na	+4.3	+4.6	+4.8 Jan	+1.7 Feb	+1.0	+1.4	3.9 Jan
Thailand	+4.2 Q4	+2.7	+4.3	+4.8	+7.3 Jan	+2.3 Feb	+5.6	+2.9	1.0 Dec
Argentina	+8.7 Q3	+10.8	+7.0	+4.8	+2.2 Jan	+9.6 Feb	+11.5	+9.8	8.7 Q4‡‡
Brazil	+3.8 Q4	+4.5	+3.3	+3.5	+4.5 Jan	+3.0 Feb	+5.5	+3.7	9.3 Jan‡‡
Chile	+2.9 Q3	−0.2	+5.1	+5.2	+3.7 Jan	+2.7 Feb	+4.1	+2.6	6.1 Jan††††
Colombia	+7.7 Q3	+8.1	+5.0	+4.5	+12.3 Dec	+5.3 Feb	+4.2	+4.2	11.8 Dec‡‡
Mexico	+4.3 Q4	+1.9	+3.5	+3.7	+1.4 Jan	+4.1 Feb	+3.7	+3.8	4.0 Jan‡‡
Venezuela	+10.2 Q3	na	+6.2	+3.9	+4.1 Dec	+20.4 Feb	+12.5	+18.3	10.1 Q3‡‡
Egypt	+7.1 Q3	na	+6.5	+5.9	+4.0 2005	+12.4 Jan	+3.4	+9.9	10.9 Q2‡‡
Israel	+3.7 Q4	+8.0	+4.6	+4.3	+10.5 Dec	+0.1 Jan	+2.7	+1.4	7.7 Q4
Saudi Arabia	+4.2 2006§	na	+4.1§	+5.0§	na	+2.9 Dec	+1.2	+2.5§	na
South Africa	+6.1 Q4	+5.6	+4.4	+4.7	+6.2 Jan	+6.0 Jan	+4.0	+5.4	25.6 Mar‡‡
MORE COUNTRIES Data for the countries below are not provided in printed editions of *The Economist*									
Estonia	+10.9 Q4	+8.2	+9.2§	+7.6§	+6.8 Jan	+4.7 Feb	+4.6	+4.3§	4.3 Dec
Finland	+5.3 Q4	+3.8	+2.7§	+2.5§	−3.2 Jan	+2.3 Jan	+0.8	+1.4§	7.0 Jan
Iceland	+2.5 Q4	+7.8	+0.4§	+2.6§	na	+5.9 Mar	+4.5	+4.9§	1.2 Dec‡‡
Ireland	+7.7 Q3	+10.8	+5.3§	+3.6§	+17.0 Dec	+5.2 Jan	+3.0	+3.4§	4.3 Feb
Latvia	+11.9 Q4	na	+9.2§	+7.5§	+0.2 Jan	+7.3 Feb	+6.1	+6.0§	6.1 Dec
Lithuania	+6.6 Q4	+6.6	+6.5§	+6.4§	na	+4.0 Jan	+3.5	+1.8§	5.7 Dec
Luxembourg	+5.4 Q3	+4.1	+4.6§	+4.1§	+4.5 Nov	+2.3 Jan	+2.9	+2.0§	4.9 Jan‡‡
New Zealand	+1.3 Q3	+1.0	+3.0§	+3.1§	−1.4 Q3	+2.6 Q4	+3.1	+2.0§	3.7 Q4
Peru	+9.0 Dec	na	+6.1	+5.5	+11.9 Dec	+0.4 Feb	+2.7	+1.4	11.6 Jan‡‡
Philippines	+6.5 Q4	+5.6	+5.6	+5.7	−9.2 Dec	+2.6 Feb	+7.6	+4.2	7.3 Q4‡‡
Portugal	+1.7 Q4	+1.9	+1.4§	+2.0§	+3.0 Jan	+2.6 Jan	+2.7	+2.4	8.2 Q4‡‡
Slovakia	+9.6 Q4	na	+6.3§	+5.4§	+17.5 Jan	+2.7 Feb	+4.4	+2.8	12.0 Dec
Slovenia	+5.5 Q4	na	+4.0§	+3.8§	+4.2 Dec	+2.1 Feb	+2.2	+2.3	8.6 Dec‡‡

*% change on previous quarter, annual rate. †The Economist poll. ‡National definitions. §Economist Intelligence Unit estimate/forecast. **RPI inflation rate 4.2% in Jan. ††Latest three months. ‡‡Not seasonally adjusted. §§Year ending June.

Sources: National statistics offices and central banks; Thomson Datastream; Reuters; Centre for Monitoring Indian Economy; OECD; ECB

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The Economist commodity-price index

Mar 15th 2007
From The Economist print edition

The Economist commodity-price index

2000=100

	Mar 6th	Mar 13th*	% change on one month	% change on one year
Dollar index				
All items	187.6	190.6	+2.9	+24.3
Food	157.0	157.5	−0.2	+17.7
Industrials				
All	227.1	233.5	+5.7	+30.6
Nfa†	152.6	153.3	−2.0	+2.8
Metals	267.7	277.2	+8.2	+42.3
Sterling index				
All items	147.7	149.6	+3.4	+12.2
Euro index				
All items	132.3	133.5	+1.4	+13.2
Gold				
$ per oz	641.82	648.90	−2.3	+18.5
West Texas Intermediate				
$ per barrel	60.72	57.97	−1.6	−7.8

*Provisional †Non-food agriculturals.

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Trade, exchange rates, budget balances and interest rates

Mar 15th 2007
From The Economist print edition

Trade, exchange rates, budget balances and interest rates

	Trade balance* latest 12 months, $bn	Current-account balance latest 12 months, $bn	Current-account balance % of GDP 2007†	Currency units, per $ Mar 14th	Currency units, per $ year ago	Budget balance % of GDP 2007‡	Interest rates, % 3-month latest	Interest rates, % 10-year gov't bonds, latest
United States	−836.1 Dec	−856.7 Q4	−5.9	–	–	−1.8	5.16	4.52
Japan	+83.9 Jan	+173.3 Jan	+3.8	116	118	−4.8	0.57	1.55
China	+204.8 Feb	+160.8 2005	+7.6	7.74	8.04	−1.7	2.82	3.19
Britain	−154.2 Jan	−69.7 Q3	−3.1	0.52	0.57	−2.7	5.50	4.73
Canada	+47.3 Jan	+21.4 Q4	+0.9	1.18	1.15	0.8	4.16	4.04
Euro area	−9.4 Dec	−20.2 Dec	−0.0	0.76	0.83	−1.2	3.87	na
Austria	−0.2 Dec	+12.2 Q3	+1.1	0.76	0.83	−1.2	3.89	3.87
Belgium	+16.5 Dec	+6.8 Sep	+2.2	0.76	0.83	0.1	3.95	3.90
France	−36.0 Jan	−31.8 Dec	−1.4	0.76	0.83	−2.5	3.89	3.88
Germany	+209.6 Jan	+152.0 Jan	+4.8	0.76	0.83	−0.8	3.89	3.83
Greece	−44.3 Dec	−29.6 Dec	−7.1†	0.76	0.83	−2.9	3.89	4.09
Italy	−26.2 Dec	−42.1 Dec	−1.9	0.76	0.83	−2.8	3.89	4.07
Netherlands	+41.4 Dec	+59.7 Q4	+7.8	0.76	0.83	0.6	3.89	3.86
Spain	−112.7 Dec	−110.7 Nov	−8.5	0.76	0.83	0.4	3.89	3.89
Czech Republic	+1.9 Jan	−6.1 Q4	−3.3	21.3	23.9	−4.2	2.57	3.74
Denmark	+6.7 Jan	+6.3 Jan	+2.8	5.63	6.20	3.5	4.08	3.85
Hungary	−2.5 Jan	−6.9 Q3	−5.0	190	218	−7.1	8.06	7.01
Norway	+56.0 Jan	+56.1 Q4	+17.5†	6.15	6.62	19.3	4.46	4.40
Poland	−5.6 Jan	−7.7 Jan	−2.3	2.95	3.22	−2.7	4.21	5.21
Russia	+138.0 Jan	+95.6 Q4	+6.0	26.1	27.8	6.0	10.50	6.40
Sweden	+20.0 Jan	+28.4 Q4	+6.1	7.03	7.79	2.9	3.20	3.67
Switzerland	+9.7 Jan	+105.9 Q3	+15.1	1.21	1.30	0.3	2.22	2.61
Turkey	−52.2 Jan	−31.9 Dec	−7.0	1.42	1.33	−2.6	19.18	20.10
Australia	−9.2 Jan	−40.9 Q4	−5.1	1.27	1.35	1.2	6.37	5.61
Hong Kong	−18.9 Jan	+19.3 Q3	+9.4	7.82	7.76	2.0	4.26	4.09
India	−54.6 Jan	−13.7 Q3	−2.3	44.3	44.4	−4.3	7.46	8.21
Indonesia	+39.7 Jan	+7.0 Q3	+1.2	9,220	9,125	−0.9	8.67	6.42§
Malaysia	+29.1 Jan	+22.2 Q3	+12.9	3.51	3.71	−4.3	3.68	5.12§
Pakistan	−13.5 Feb	−6.5 Q4	−4.8†	60.7	60.2	−4.7	10.18	6.67§
Singapore	+34.4 Jan	+36.3 Q4	+23.5	1.53	1.62	0.3	3.06	2.88
South Korea	+17.3 Feb	+5.5 Jan	+0.3	946	975	0.4	4.94	4.88
Taiwan	+13.8 Feb	+25.2 Q4	+5.9	33.0	32.4	−2.2	1.82	2.05
Thailand	+2.2 Dec	+3.2 Dec	+1.9	33.1	39.2	−1.4	4.65	4.15
Argentina	+12.0 Jan	+6.7 Q3	+2.4	3.10	3.07	1.1	9.63	na
Brazil	+45.8 Feb	+14.2 Jan	+0.7	2.11	2.12	−3.2	12.68	6.16§
Chile	+24.4 Feb	+5.2 Q3	+0.8	540	528	4.3	5.04	5.13§
Colombia	−0.1 Dec	−2.3 Q3	−2.3	2,209	2,260	−1.4	7.28	6.12§
Mexico	−8.2 Jan	−1.5 Q4	−1.2	11.2	10.7	−0.6	7.05	7.79
Venezuela	+33.0 Q4	+27.2 Q4	+9.3	3,816	2,499	−3.8	10.13	6.55§
Egypt	−11.7 Q3	+3.0 Q3	+1.3	5.70	5.74	−7.6	8.37	5.28§
Israel	−7.7 Feb	+6.8 Q4	+3.4	4.21	4.71	−2.7	4.37	4.95
Saudi Arabia	+165.7 2006	+90.0 2005	+17.3†	3.75	3.75	12.3	5.12	na
South Africa	−10.2 Jan	−13.5 Q3	−5.3	7.48	6.19	−2.0	9.20	7.66
MORE COUNTRIES	Data for the countries below are not provided in printed editions of *The Economist*							
Estonia	−3.4 Dec	−2.3 Dec	−13.9†	11.8	13.0	1.5	3.97	na
Finland	+12.1 Dec	+12.8 Jan	+5.6†	0.76	0.83	2.3	3.86	3.90
Iceland	−2.1 Jan	−4.4 Q4	−19.7†	67.3	70.0	0.8	13.63	na
Ireland	+35.5 Dec	−6.5 Q3	−4.2†	0.76	0.83	0.8	3.89	3.87
Latvia	−5.0 Dec	−4.3 Dec	−19.5†	0.54	0.58	−1.2	5.12	na
Lithuania	−5.4 Jan	−3.4 Dec	−10.3†	2.61	2.87	−0.5	3.99	na
Luxembourg	−5.2 Dec	+4.8 Q3	na	0.76	0.83	−0.8	3.89	na
New Zealand	−4.0 Jan	+6.1 Q3	−9.6†	1.45	1.55	3.5	6.75	5.80
Peru	+8.7 Jan	+2.5 Q4	+1.0	3.18	3.33	0.3	4.50	na
Philippines	−4.5 Dec	+4.4 Sep	+3.2	48.7	51.0	−1.0	5.31	na
Portugal	−23.2 Nov	−18.2 Dec	−7.8†	0.76	0.83	−3.7	3.89	4.03
Slovakia	−2.7 Jan	−5.4 Nov	−6.2†	25.7	31.2	−3.0	4.20	4.31
Slovenia	−2.1 Jan	−1.2 Dec	−1.6†	0.76	0.83	−1.2	na	na

*Merchandise trade only. †The Economist poll. ‡Economist Intelligence Unit forecast. §Dollar-denominated bonds.

Sources: National statistics offices and central banks; Thomson Datastream; Reuters; JPMorgan; Bank Leumi le-Israel; Centre for Monitoring Indian Economy; Danske Bank; Hong Kong Monetary Authority; Standard Bank Group; UBS; Westpac.

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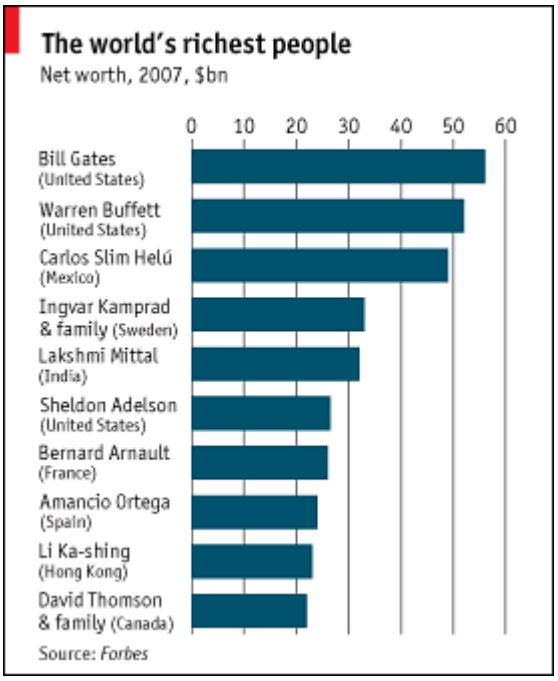
The world's richest people

Mar 15th 2007
From The Economist print edition

The very rich are different from you and me, wrote F. Scott Fitzgerald. Quite how different they have become in recent years emerges in an international tally by *Forbes*. The business magazine has counted a record 946 billionaires around the world, with a combined net worth of $3.5 trillion. Heading the list are the familiar names of Bill Gates and Warren Buffett, both Americans. However, seven of the world's ten richest people are citizens of countries other than the United States. Newcomers to the club include 19 Russians, 14 Indians, 13 Chinese and ten Spaniards. The billionaire boom reflects the big rise in global wealth thanks to strong equity and property markets and buoyant commodity prices.



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About sponsorship

Markets

Mar 15th 2007
From The Economist print edition

Markets

	Index Mar 14th	% change on one week	% change on Dec 29th 2006 in local currency	% change on Dec 29th 2006 in $ terms
United States (DJIA)	12,133.4	–0.5	–2.6	–2.6
United States (S&P 500)	1,387.2	–0.3	–2.2	–2.2
United States (NAScomp)	2,371.7	–0.1	–1.8	–1.8
Japan (Nikkei 225)	16,676.9	–0.5	–3.2	–1.4
Japan (Topix)	1,674.9	–0.9	–0.4	+1.5
China (SSEA)	3,053.6	+0.3	+8.5	+9.3
China (SSEB, $ terms)	169.9	–0.5	+29.5	+30.6
Britain (FTSE 100)	6,000.7	–2.5	–3.5	–4.8
Canada (S&P TSX)	12,808.7	–1.4	–0.8	–1.2
Euro area (FTSE Euro 100)	1,231.2	–2.6	–3.7	–3.6
Euro area (DJ STOXX 50)	3,906.1	–2.9	–5.2	–5.1
Austria (ATX)	4,325.4	–1.0	–3.1	–3.0
Belgium (Bel 20)	4,196.6	–2.4	–4.4	–4.3
France (CAC 40)	5,296.2	–2.9	–4.4	–4.3
Germany (DAX)*	6,447.7	–2.6	–2.3	–2.2
Greece (Athex Comp)	4,402.5	–1.5	+0.2	+0.3
Italy (S&P/MIB)	39,290.0	–2.7	–5.2	–5.1
Netherlands (AEX)	473.4	–1.8	–4.4	–4.3
Spain (Madrid SE)	1,509.6	–2.3	–2.9	–2.8
Czech Republic (PX)	1,628.4	+0.1	+2.5	+0.1
Denmark (OMXCB)	424.1	–0.8	nil	+0.1
Hungary (BUX)	23,063.1	+2.4	–7.2	–6.5
Norway (OSEAX)	491.8	–0.6	–2.1	–0.6
Poland (WIG)	52,873.5	+2.8	+4.9	+3.3
Russia (RTS, $ terms)	1,779.1	+0.7	–8.0	–7.4
Sweden (Aff.Gen)	361.9	–2.3	–0.9	–3.6
Switzerland (SMI)	8,577.7	–3.4	–2.4	–2.4
Turkey (ISE)	40,501.9	+0.2	+3.5	+3.8
Australia (All Ord.)	5,727.3	–1.3	+1.5	+0.4
Hong Kong (Hang Seng)	18,836.9	–0.4	–5.6	–6.1
India (BSE)	12,529.6	–0.4	–9.1	–9.0
Indonesia (JSX)	1,762.3	+1.1	–2.4	–4.7
Malaysia (KLSE)	1,166.4	+0.8	+6.4	+7.0
Pakistan (KSE)	11,280.3	+1.2	+12.3	+12.7
Singapore (STI)	3,053.2	–0.2	+2.3	+2.6
South Korea (KOSPI)	1,407.4	–0.3	–1.9	–3.4
Taiwan (TWI)	7,570.3	+1.2	–3.2	–4.4
Thailand (SET)	670.6	nil	–1.4	+8.1
Argentina (MERV)	2,011.5	+0.8	–3.8	–4.9
Brazil (BVSP)	43,288.0	+1.5	–2.7	–0.6
Chile (IGPA)	13,060.8	+0.3	+5.6	+4.3
Colombia (IGBC)	10,199.0	+0.1	–8.6	–7.2
Mexico (IPC)	26,719.3	+2.0	+1.0	–2.0
Venezuela (IBC)	50,295.5	–2.8	–3.7	–10.4
Egypt (Hermes)	63,372.7	+3.1	+3.4	+3.6
Israel (TA-100)	960.6	+0.2	+4.2	+4.6
Saudi Arabia (Tadawul)	8,603.1	–1.9	+7.6	+7.7
South Africa (JSE AS)	25,250.1	–0.1	+1.3	–3.7
Europe (FTSEurofirst 300)	1,427.4	–2.7	–3.8	–3.7
World, dev'd (MSCI)	1,456.2	–1.0	–1.8	–1.8
Emerging markets (MSCI)	872.3	+0.7	–4.4	–4.4
World, all (MSCI)	360.2	–0.8	–2.1	–2.1
World bonds (Citigroup)	670.6	+0.5	+1.9	+1.9
EMBI+ (JPMorgan)	414.4	+0.3	+1.7	+1.7
Hedge funds (HFRX)	1,283.1	+0.1	+0.6	+0.6
Volatility, US (VIX)	17.3	15.2	11.6	(levels)
CDSs, Eur (iTRAXX)†	21.3	+4.3	–0.6	–0.5
CDSs, N Am (CDX)†	31.6	–4.7	+7.4	+7.4
Carbon trading (EU ETS) €	1.11	+20.7	–82.4	–82.4

*Total return index. †Credit-default swap spreads, basis points.

Sources: National statistics offices, central banks and stock exchanges; Thomson Datastream; Reuters; WM/Reuters; JPMorgan Chase; Bank Leumi le-Israel; CBOE; CME; Danske Bank; EEX; HKMA; Markit; Standard Bank

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